U.S. $2,000,000,000

TENNESSEE VALLEY AUTHORITY

5⅜% Global Power Bonds 1998 Series G Due November 13, 2008

Interest Payable May 13 and November 13

The 5⅜% Global Power Bonds 1998 Series G Due November 13, 2008 (the "Bonds") of the Tennessee Valley Authority ("TVA") will not be subject to redemption prior to maturity. The Bonds will be issued in minimum denominations of U.S.$1,000 and integral multiples thereof.

The Bonds will be issued, maintained and transferred only on the book-entry system of the U.S. Federal Reserve Banks, as described herein. Transactions in the Bonds will be cleared and settled in book-entry form by Euromarket participants through the facilities of Cedel Bank (as defined herein) and Euroclear (as defined herein). See "Clearance and Settlement". The Bonds will not be exchangeable for definitive securities.

The Bonds may be separated ("stripped") into their separate Interest and Principal Components (as defined herein) and maintained as such on the book-entry records of the U.S. Federal Reserve Banks. The components of each stripped Bond are: each future interest payment (each an "Interest Component") and the principal payment (the "Principal Component" and, together with the Interest Components, hereinafter collectively referred to as the "Strips"). See "Description of Bonds" — "Stripping" and "United States Tax Matters".

Application has been made to list the Bonds on the Luxembourg Stock Exchange, The Stock Exchange of Hong Kong Limited (the "Hong Kong Stock Exchange"), the Stock Exchange of Singapore Limited (the "Singapore Stock Exchange") and the New York Stock Exchange (collectively, the "Stock Exchanges"). Application also has been made to list the Strips on the Luxembourg Stock Exchange. It is expected that dealings in the Bonds on the Hong Kong Stock Exchange will commence on or about November 16, 1998.

The Bonds and Strips are considered to be obligations in registered form for United States federal tax purposes. Beneficial owners of the Bonds or Strips that are not United States persons must certify that they are non-United States persons in order to receive payments on those Bonds or Strips free of United States withholding tax. See "United States Tax Matters". TVA will not pay additional interest or other amounts in respect of any withholding or other tax that may be imposed by any jurisdiction on payments on the Bonds or Strips as a result of a change in law or otherwise.

TVA is a wholly owned corporate agency and instrumentality of the United States of America. Principal and interest will be payable solely from TVA's Net Power Proceeds (as defined herein).

THE BONDS WILL NOT BE OBLIGATIONS OF, NOR WILL PAYMENT OF THE PRINCIPAL THEREOF OR THE INTEREST THEREON BE GUARANTEED BY, THE UNITED STATES OF AMERICA. THE BONDS ARE NOT REQUIRED TO BE REGISTERED UNDER THE U.S. SECURITIES ACT OF 1933. ACCORDINGLY, NO REGISTRATION STATEMENT HAS BEEN FILED WITH THE U.S. SECURITIES AND EXCHANGE COMMISSION. TVA IS NOT SUBJECT TO THE PERIODIC REPORTING REQUIREMENTS OF THE U.S. SECURITIES EXCHANGE ACT OF 1934.

	Price to Public(1)	Discount to Managers	Proceeds to TVA(1)(2)
Per Bond	99.580%	0.325%	99.255%
Total	U.S.$1,991,600,000	U.S.$6,500,000	U.S.$1,985,100,000

(1) Plus accrued interest, if any, from November 13, 1998 to date of delivery.
(2) Before deducting expenses payable by TVA estimated at U.S. $450,000.

The Bonds offered by this Offering Circular are offered by the several Managers (as defined herein) subject to prior sale, withdrawal, cancellation or modification of the offer without notice, to delivery to and acceptance by the Managers and to certain further conditions. It is expected that delivery of the Bonds, in book-entry form, will be made through the book-entry system of the U.S. Federal Reserve Banks on or about November 13, 1998, against payment therefor in immediately available funds.

LEHMAN BROTHERS   J.P. MORGAN & CO.

CREDIT SUISSE FIRST BOSTON   DEUTSCHE BANK
FIRST TENNESSEE BANK N.A.   GOLDMAN, SACHS & CO.
MORGAN STANLEY DEAN WITTER

November 6, 1998

GLOBAL IMPACT

TVA is recognized around the world as an expert in power production, flood control, river navigation, and environmental quality. Many international visitors come to TVA each year to study its river operations and power program. TVA has hosted representatives from countries such as Australia, Brazil, Sri Lanka, China, Estonia, France, Germany, India, Japan, Malaysia, Poland, Russia, Sweden, and Tanzania.

Southeastern Region Served by the Tennessee Valley Authority

Countries around the globe have come to depend on TVA's knowledge and experience in the utility industry and in resource management. For example:

- The Republic of Georgia is receiving assistance from TVA in analyzing its energy needs. Georgia's Energy Department is a sister utility to TVA as part of a program funded by the United States Agency for International Development.

- The People's Republic of China is using TVA's expertise in developing the Yellow and Yalong rivers for flood control, hydroelectric power, industrial development, and farming. In fact, China is using TVA as a model.

- TVA has been involved in the study phases of river development programs in Lesotho, South Africa, the Nile in Sudan, Lake Titicaca located between Bolivia and Peru, and Zimbabwe.

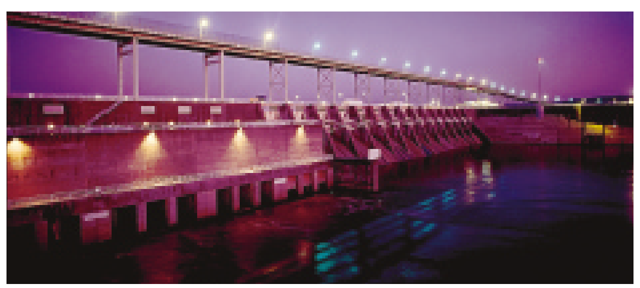
These are just a few of the reasons why TVA has an international reputation for teamwork, innovation, and dependability.

U.S. Ambassador to the People's Republic of China Jim Sasser (left) greets TVA Chairman Craven Crowell at a reception at the U.S. Embassy in Beijing in conjunction with Tennessee Valley Authority's and the State of Tennessee's international conference on economic development and energy.

TVA

PROVIDING POWER IN THE PUBLIC INTEREST

TVA is poised to be a major player in what is predicted to be a new, highly competitive electric utility market. With one of the largest generating and transmission systems in the United States, TVA's power operations form a vital part of the nation's energy infrastructure.

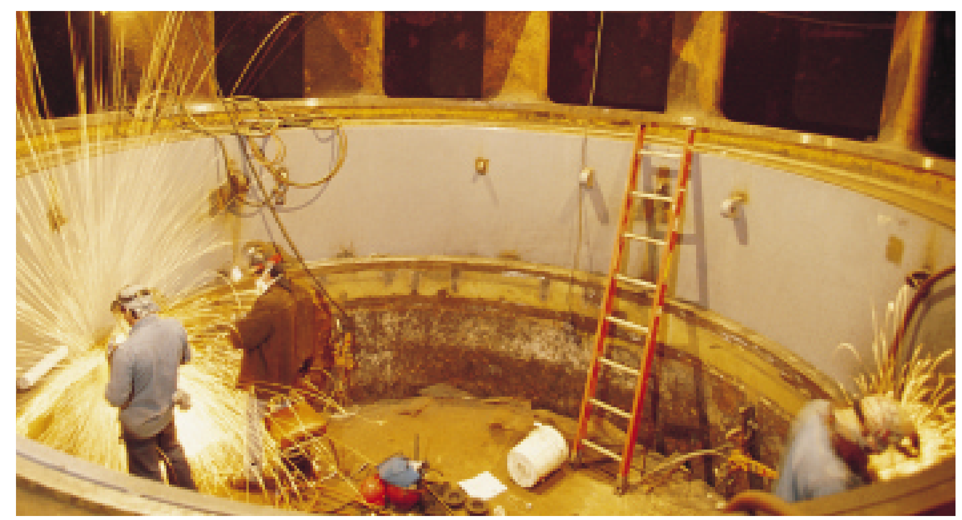


TVA provides reliable, universal access to electricity at competitive prices and provides stewardship of the lands and waters of the Tennessee River Valley. TVA power enriches lives, promotes economic growth, and improves the overall quality of life in the Tennessee Valley.

TVA's power system is entirely self-funded and not supported by any U.S. federal tax dollars. The power system is running better today than at any time in the past decade. TVA has made substantial improvements to its nuclear program over the last decade, restarting four nuclear units, completing and starting a fifth and bringing its total nuclear generation to over 40 billion kWh in fiscal 1997. TVA's fossil and hydro plants increased their productivity by about 20 percent systemwide between fiscal 1994 and 1997. TVA carries out other programs mandated by the U.S. Congress, such as economic development, flood control, navigation and natural resource development on the Tennessee River.

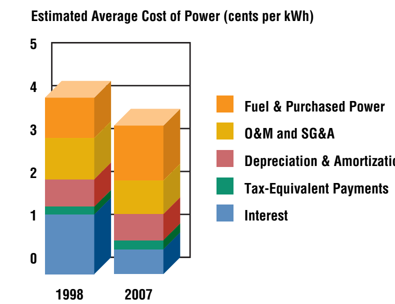
TVA unveiled an ambitious 10-year Business Plan in July 1997 that is designed to strengthen it financially, position the electric power operations to meet the competitive challenges of a restructured marketplace, promote economic development and provide power to its customers at the lowest feasible rates. This plan sets a focused course for TVA to reduce its debt by half by 2007 and lower its average cost of power to 3.5 cents per kilowatt hour.

The 10-year Business Plan is designed to accomplish long-term objectives that would enable TVA to be competitive in the coming restructured marketplace by:



- Reducing the cost of power as needed to meet the lower market prices anticipated in a more competitive market.
- Altering TVA's cost structure from a high fixed-to-variable cost relationship to a more flexible structure better suited to a volatile, competitive market.
- Strengthening customer allegiance and satisfaction by developing opportunities for mutual support and partnerships.

TVA is committed to serving the public good–through economic development, reliable service, environmental stewardship and universal access. TVA, as a government owned power entity, is an advocate for the public interest in electricity generation, transmission and distribution as the electric utility industry is restructured.



TVA targets reducing its cost of power from 4.1 cents per kWh in 1998 to 3.5 cents by 2007.

LEHMAN BROTHERS INTERNATIONAL (EUROPE) MAY ENGAGE IN TRANSACTIONS THAT STABILIZE, MAINTAIN, OR OTHERWISE AFFECT THE PRICE OF THE BONDS. SPECIFICALLY, LEHMAN BROTHERS INTERNATIONAL (EUROPE) MAY OVERALLOT IN CONNECTION WITH THE OFFERING, AND MAY BID FOR, AND PURCHASE, BONDS IN THE OPEN MARKET AND MAY IMPOSE PENALTY BIDS. SUCH TRANSACTIONS MAY BE EFFECTED ON THE LUXEMBOURG STOCK EXCHANGE AND/OR THE NEW YORK STOCK EXCHANGE, IN AN OVER-THE-COUNTER MARKET OR OTHERWISE.

None of the Stock Exchanges takes any responsibility for the correctness of any statements made or opinions expressed in this Offering Circular or any other document incorporated by reference herein or makes any representation as to its accuracy or completeness. Each of the Stock Exchanges expressly disclaims any liability whatsoever for any loss howsoever arising from or in reliance upon the whole or any part of this Offering Circular or any other document incorporated by reference herein. Neither an admission to the official lists of, or quotation of, or permission to deal in, the Bonds on any of the Stock Exchanges is to be taken as an indication of the merits of TVA or the Bonds.

No dealer, salesperson or any other person has been authorized by TVA to give any information or to make any representations on behalf of TVA other than those contained in this Offering Circular, the current Information Statement (as defined herein), or any supplement to any of the foregoing prepared by TVA for use in connection with the offer made by this Offering Circular and, if given or made, such information or representations must not be relied upon as having been authorized by TVA. Neither the delivery of this Offering Circular or the current Information Statement nor any sale of Bonds described herein shall under any circumstances create an implication that the information provided herein is correct at any time subsequent to its date, and TVA assumes no duty to update this Offering Circular except as it deems appropriate. TVA assumes no duty to update the current Information Statement, except as described therein. This Offering Circular does not constitute an offer to sell or a solicitation of an offer to buy the Bonds described herein in any jurisdiction to any person to whom it is unlawful to make such offer or solicitation in such jurisdiction.

The distribution of this Offering Circular and the offering of the Bonds may, in certain jurisdictions, be restricted by law. Persons into whose possession this Offering Circular comes are required by TVA and the Managers to inform themselves of and observe all such restrictions.

This Offering Circular should be read in conjunction with TVA's current Information Statement, dated February 27, 1998 (the "current Information Statement"), which is attached hereto and incorporated herein. Any statement contained in the current Information Statement shall be deemed to be modified or superseded for all purposes of the current Information Statement and this Offering Circular to the extent that a statement contained in this Offering Circular modifies or supersedes such statement. Any statement so modified or superseded shall not be deemed, except as so modified, to constitute a part of the current Information Statement. Additional copies of this Offering Circular and of the current Information Statement may be obtained (free of charge) upon written request directed to Tennessee Valley Authority, 400 West Summit Hill Drive, Knoxville, Tennessee 37902, Attention: Vice President and Treasurer, or by calling (423) 632-3366 in the United States. Copies may also be obtained (free of charge) from Kredietbank S.A. Luxembourgeoise (the "Special Agent" or "Listing Agent"), 43 Boulevard Royal L-2955, Luxembourg, R.C. Luxembourg B6395. Copies may be inspected upon request during normal business hours (Saturdays, Sundays and public holidays excepted) for a period of fourteen days from the date hereof at the offices of Allen & Overy, 9th floor, Three Exchange Square, Central, Hong Kong and at the offices of Allen & Gledhill, 36 Robinson Road, #18-01, City House, Singapore. The then-current Information Statement and other information concerning TVA may be inspected at the offices of the New York Stock Exchange, 20 Broad Street, New York, New York 10005.

This Offering Circular has been prepared by TVA solely for use in connection with the offering of the Bonds described herein and for purposes of listing the Bonds on the Stock Exchanges. TVA has taken reasonable care to ensure that the information contained in this Offering Circular is true and accurate in all material respects and that there are no material facts the omission of which would make misleading any statements herein, in light of the circumstances under which such statements are made. TVA accepts responsibility accordingly.

In this Offering Circular and the current Information Statement, references to "U.S. dollars", "U.S. $", "dollars" and "$" are to United States dollars.

FORWARD-LOOKING STATEMENTS

This Offering Circular and the current Information Statement contain forward-looking statements relating to future events and future performance. Any statements regarding expectations, beliefs, plans, projections, estimates, objectives, intentions or assumptions or otherwise relating to future events or performance may be forward-looking. Some examples include statements regarding TVA's projections of future power and energy requirements, future costs related to environmental compliance, targets for TVA's future competitive position and the potential effect of the Year 2000 issue on TVA's operations. Although TVA believes that these statements are accurate, TVA does not guarantee their accuracy. Numerous factors could cause actual results to differ materially from those in the forward-looking statements. Such factors include, among other things, new laws and regulations, especially those related to the deregulation of electric utilities, the status of TVA as a government agency and various environmental matters; increased competition among electric utilities; legal and administrative proceedings affecting TVA; the financial environment; performance of TVA's generating facilities; fuel prices; the demand for electricity; weather conditions; changes in accounting standards; the efficacy of TVA's Year 2000 remediation efforts and the efforts of those entities with which it interfaces; and unforeseeable adverse events.

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Offering Circular

Information Statement

SUMMARY OF OFFERING

The information below is qualified in its entirety by the detailed information appearing in TVA's current Information Statement (and any supplement thereto) and elsewhere in this Offering Circular. Capitalized terms used and not defined herein have the meanings defined in such Information Statement and elsewhere in this Offering Circular.

Issuer	TVA is a wholly owned corporate agency and instrumentality of the United States of America established by the Tennessee Valley Authority Act of 1933, as amended.
Capitalization	Total capitalization of TVA at June 30, 1998, as adjusted for the Bonds offered hereby, would have been U.S.$30,327 million. In addition, since June 30, 1998 and through the date of this Offering Circular, TVA has issued U.S.$1,050 million of long-term debt to retire existing debt. Except as set forth above, there has been no material change in TVA's capitalization since June 30, 1998.
Securities Offered	U.S.$2,000,000,000 aggregate principal amount of 5⅜% Global Power Bonds 1998 Series G Due November 13, 2008 (the "Bonds")
Interest	The Bonds will bear interest from November 13, 1998, at the annual rate set forth on the cover page hereof, payable semiannually in arrear on each May 13 and November 13, commencing May 13, 1999.
Redemption	The Bonds will not be subject to redemption prior to maturity.
Fiscal Agent	U.S. Federal Reserve Banks
Listings	Application has been made to list the Bonds on the Luxembourg Stock Exchange, the Hong Kong Stock Exchange, the Singapore Stock Exchange and the New York Stock Exchange. Application also has been made to list the Strips on the Luxembourg Stock Exchange.
Use of Proceeds	The net proceeds received by TVA from the sale of the Bonds will be used to retire existing debt.
Source of Payment	The interest and principal on the Bonds are payable solely from Net Power Proceeds and are not obligations of, or guaranteed by, the United States of America. See "The Basic Resolution; Power Bonds, Discount Notes and Other Indebtedness" in the current Information Statement.
Form and Denomination of Bonds	The Bonds will be issued and maintained and may be transferred by Holders (as defined herein) only on the book-entry system of the U.S. Federal Reserve Banks. See "Description of Bonds" — "Book-Entry System". The Bonds will not be exchangeable for definitive securities. The Bonds will be issued and must be maintained and transferred in minimum denominations of U.S.$1,000 and integral multiples thereof.
Stripping	The Bonds may be stripped into their separate Interest and Principal Components and maintained as such on the book-entry records of the U.S. Federal Reserve Banks. The components of each stripped Bond are: each future interest payment and the principal payment. Each Interest Component and the Principal Component will have an identifying designation and CUSIP number. See "Description of Bonds" — "Stripping" and "United States Tax Matters", and see "The Basic Resolution; Power Bonds, Discount Notes and

Other Indebtedness" — "Stripping" in the current Information Statement.

Delivery of Strips . . . . The Managers immediately upon their acceptance of the Bonds may, but are not obligated to, strip some or all of the Bonds and deliver Strips rather than Bonds to investors purchasing Strips. Sales of any such Strips would be at negotiated prices. See "Subscription and Selling".

Clearance and Settlement . . . . The Bonds may be held in accounts with institutions having access in the United States to the book-entry system of the U.S. Federal Reserve Banks. Transactions in the Bonds will be cleared and settled by Euromarket participants through the facilities of Cedel Bank and Euroclear. See "Clearance and Settlement".

Legality of Investment in the United States . . . . Each person or entity is advised to consult with its own counsel with respect to the legality of investment in the Bonds or in any stripped Interest and Principal Components thereof, which could be subject to restrictions or requirements that do not apply to Power Bonds held in their fully constituted form.

The following generally describes the legality of investment in the United States in TVA Power Bonds in their fully constituted form. Power Bonds are:

- acceptable as security for all fiduciary, trust, and public funds, the investment or deposit of which shall be under the authority or control of any officer or agency of the United States of America;
- among those obligations which U.S. national banks may deal in, underwrite and purchase for their own accounts in an amount up to 10% of unimpaired capital and surplus;
- eligible as collateral for advances by U.S. Federal Reserve Banks to member banks;
- legal investments for U.S. federal savings associations and U.S. federal savings banks to the extent specified in applicable regulations;
- eligible as collateral for advances by U.S. Federal Home Loan Banks to members for which Power Bonds are legal investments; and
- legal investments for U.S. federal credit unions.

See "Legality of Investment in the United States".

No Acceleration Rights . . . . The Bonds will not contain any provisions permitting the Holders to accelerate the maturity thereof on the occurrence of any default or other event.

Taxation . . . . United States federal income tax generally will not be withheld from payments on Bonds or Strips that are beneficially owned by non-U.S. beneficial owners (as defined under "United States Tax Matters"), provided that an appropriate United States Internal Revenue Service Form W-8 (or successor form) is provided. See "United States Tax Matters". The Bonds are not subject to redemption by reason of the imposition of withholding or other tax by any jurisdiction, and TVA will have no obligation to pay additional interest or other amounts in respect of any such tax that may be imposed on payments on the Bonds or Strips as a result of a change in law or otherwise, including any withholding tax that may be imposed as a result of a failure to provide an applicable United States Internal Revenue Service form.

For further discussion of United States tax consequences with respect to the purchase, ownership or disposition of the Bonds and Strips, see "United States Tax Matters".

Common Code	9226591
ISIN	US880591 DB53
CUSIP Number	880591 DB5

If the Bonds are stripped into their separate Interest and Principal Components, the following Common Code, ISIN and CUSIP numbers will apply:

Interest Components	Common Code	ISIN	CUSIP
May 13, 1999	9229884	US88059E QU19	88059E QU1
November 13, 1999	9229914	US88059E QV91	88059E QV9
May 13, 2000	9229957	US88059E QW74	88059E QW7
November 13, 2000	9229973	US88059E QX57	88059E QX5
May 13, 2001	9229990	US88059E QY31	88059E QY3
November 13, 2001	9230033	US88059E QZ06	88059E QZ0
May 13, 2002	9230050	US88059E RA46	88059E RA4
November 13, 2002	9230106	US88059E RB29	88059E RB2
May 13, 2003	9230114	US88059E RC02	88059E RC0
November 13, 2003	9230068	US88059E RD84	88059E RD8
May 13, 2004	9230408	US88059E RE67	88059E RE6
November 13, 2004	9230092	US88059E RF33	88059E RF3
May 13, 2005	9230165	US88059E RG16	88059E RG1
November 13, 2005	9230173	US88059E RH98	88059E RH9
May 13, 2006	9230181	US88059E RJ54	88059E RJ5
November 13, 2006	9230203	US88059E RK28	88059E RK2
May 13, 2007	9230238	US88059E RL01	88059E RL0
November 13, 2007	9230246	US88059E RM83	88059E RM8
May 13, 2008	9230289	US88059E RN66	88059E RN6
November 13, 2008	9230319	US88059E RP15	88059E RP1
Principal Component	9229868	US88059F BD24	88059F BD2

TENNESSEE VALLEY AUTHORITY

The Tennessee Valley Authority is one of the largest power producers in the United States of America, having produced over 155 billion kilowatt-hours ("kWh") of electricity in fiscal 1998. The TVA system supplies electric power to a region containing nearly eight million people located in parts of Tennessee, Kentucky, Mississippi, Alabama, Georgia, North Carolina and Virginia.

TVA is a wholly owned corporate agency and instrumentality of the United States of America established pursuant to the Tennessee Valley Authority Act of 1933, as amended (the "Act"), primarily to develop and manage the resources of the Tennessee Valley region. The programs at TVA consist of power and nonpower programs. The Act requires TVA's electric system operations to be self-supporting from power system revenues, which were about U.S.$6.7 billion in fiscal 1998. Congress does not appropriate funds to TVA for its power program. The Act authorizes TVA to issue Evidences of Indebtedness (as defined in "Description of Bonds"), the proceeds of which TVA may only use to finance its power program. TVA's nonpower activities include responsibilities associated with operation of the Tennessee River System, land management, economic development and the environment. Congress provided U.S.$70 million for TVA's nonpower programs in fiscal 1998. Appropriations legislation enacted in October 1997 anticipates no further appropriations to TVA in fiscal years following 1998. Nonetheless, Congress appropriated U.S.$50 million for TVA's nonpower programs in fiscal 1999. See "Recent Developments" — "Other Matters" in this Offering Circular and "The Basic Resolution; Power Bonds, Discount Notes, and Other Indebtedness" — "Recent Legislation" in the current Information Statement.

For over six decades, TVA has been associated with bringing prosperity to a significant region of the United States. Its dams have averted an estimated U.S.$4 billion in flood damage; its power program has brought electricity to a large undeveloped area of the country; and its economic development program has contributed to a vast increase in the number of jobs in the Tennessee Valley.

Electric power industry restructuring is changing the way TVA and utilities across the nation generate, transmit and distribute electricity. TVA is positioning itself to successfully compete in a restructured marketplace by sustaining excellent operational performance and achieving greater financial flexibility. For 1997, TVA ranked as the third lowest-cost producer among the nation's largest 25 generating utilities according to information published in the October 1998 issue of *Electric Light & Power* magazine. Building on its operational soundness, TVA implemented its Ten-Year Business Plan in October 1997 to reduce its total delivered cost of power consistent with the forecast future market price of power and adopt a more flexible cost structure suitable for an increasingly volatile marketplace. See "Competition" in the current Information Statement.

TVA is an advocate for the public's interest in universal access, customer service and reliability, economic development and environmental protection. TVA will continue to work actively with Congress to ensure that these standards are upheld through the development of an equitable, effective framework for success in a restructured marketplace.

USE OF PROCEEDS

TVA will use the net proceeds from the sale of the Bonds to retire existing debt.

RECENT DEVELOPMENTS

Recent Results

Net income for fiscal 1998 amounted to U.S.$233 million, up from U.S.$8 million in fiscal 1997. Operating revenues for fiscal 1998 amounted to U.S.$6,729 million compared with U.S.$5,934 for the same period of the previous year. The increase in earnings and revenues resulted primarily from a rate increase effective October 1, 1997, coupled with revenue generated as a result of abnormally hot weather during the summer of 1998. Operating expenses increased U.S.$469 million during fiscal 1998 from U.S.$4,080 million for fiscal 1997. In addition, fiscal 1998 cash flows from operations of U.S.$1,394 million reflects an increase of 31 percent over fiscal 1997. While complete financial statements for fiscal 1998 are not available, TVA believes that these amounts reflect all adjustments necessary for fair presentation.

Financial Results

TVA has derived the condensed financial statements for TVA's power program for the fiscal years ended September 30, 1997 and 1996 from TVA's audited financial statements. The condensed financial statements for TVA's power program for the nine months ended June 30, 1998 and 1997 are unaudited but in the opinion of management of TVA include all adjustments (consisting only of normal recurring adjustments) necessary for the fair presentation of results for such periods. You should read the following information together with the audited financial statements and notes thereto in the current Information Statement. Results for the nine months ended June 30, 1998 and for past years are not necessarily indicative of future results.

TENNESSEE VALLEY AUTHORITY
POWER PROGRAM

CONDENSED BALANCE SHEETS
At June 30, 1998 and September 30, 1997

	June 30, 1998	September 30, 1997
	(Millions)	
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	U.S.$ 241	U.S.$ 299
Accounts receivable	764	701
Inventories and other, at average cost	457	399
Total current assets	1,462	1,399
PROPERTY, PLANT, AND EQUIPMENT		
Completed plant	28,850	28,528
Less accumulated depreciation	(7,736)	(7,178)
Net completed plant	21,114	21,350
Construction in progress	547	605
Deferred nuclear generating units	6,309	6,303
Nuclear fuel and capital lease assets	940	1,040
Total property, plant, and equipment	28,910	29,298
INVESTMENT FUNDS	656	561
DEFERRED CHARGES AND OTHER ASSETS(1)	2,548	2,426
Total assets	U.S.$33,576	U.S.$33,684
LIABILITIES AND PROPRIETARY CAPITAL		
CURRENT LIABILITIES		
Accounts payable	U.S.$ 470	U.S.$ 468
Accrued liabilities	149	161
Accrued interest	432	499
Short-term debt	1,731	2,151
Current maturities of long-term debt	1,703	574
Total current liabilities	4,485	3,853
OTHER LIABILITIES(1)	2,198	1,704
LONG-TERM DEBT		
Public bonds — senior	19,076	20,354
Federal Financing Bank — senior	3,200	3,200
Public bonds — subordinated	1,100	1,100
Unamortized discount and other adjustments	(500)	(502)
Total long-term debt	22,876	24,152
PROPRIETARY CAPITAL		
Appropriation investment	573	588
Retained earnings reinvested in power program	3,444	3,387
Total proprietary capital	4,017	3,975
Total liabilities and proprietary capital	U.S.$33,576	U.S.$33,684

(1) Effective October 1, 1997 TVA changed its method of accounting for decommissioning costs and related liabilities. See "Nuclear Power Program" — "Decommissioning" in the current Information Statement. The effect of the change for the nine months ended June 30, 1998 was to increase Deferred Charges and Other Assets by U.S.$384 million, increase Other Liabilities by U.S.$438 million and increase Depreciation and Amortization by U.S.$54 million.

TENNESSEE VALLEY AUTHORITY
POWER PROGRAM

CONDENSED STATEMENTS OF OPERATIONS AND RETAINED EARNINGS
For the Nine Months Ended June 30, 1998 and 1997 and for the Years Ended September 30, 1997 and 1996

	Nine Months Ended June 30,		Years Ended September 30,	
	1998	1997	1997	1996
	(Millions)			
OPERATING REVENUES				
Sales of electricity				
Municipalities and cooperatives	U.S.$3,903	U.S.$3,442	U.S.$4,811	U.S.$4,980
Industries directly served	377	340	464	452
Federal agencies	128	136	179	172
Other	55	61	98	89
Total operating revenues	4,463	3,979	5,552	5,693
OPERATING EXPENSES				
Fuel and purchased power, net	981	817	1,211	1,278
Operating and maintenance	945	894	1,201	1,218
Depreciation and amortization(1)	776	733	1,014	904
Tax-equivalents	197	202	272	256
Total operating expenses	2,899	2,646	3,698	3,656
OPERATING INCOME	1,564	1,333	1,854	2,037
OTHER INCOME (EXPENSE), NET	(3)	(5)	157	(10)
Income before interest charges	1,561	1,328	2,011	2,027
INTEREST CHARGES				
Interest expense	1,515	1,566	2,084	2,083
Allowance for funds used during construction	(41)	(62)	(81)	(117)
Net interest charges	1,474	1,504	2,003	1,966
NET INCOME (LOSS)	87	(176)	8	61
Return on appropriation investment	(30)	(31)	(41)	(43)
Increase (decrease) in retained earnings	57	(207)	(33)	18
Retained earnings reinvested at beginning of period	3,387	3,420	3,420	3,402
Retained earnings reinvested at end of period	U.S.$3,444	U.S.$3,213	U.S.$3,387	U.S.$3,420

(1) See Note (1) to Condensed Balance Sheets.

TENNESSEE VALLEY AUTHORITY
POWER PROGRAM

CONDENSED STATEMENTS OF CASH FLOWS
For the Nine Months Ended June 30, 1998 and 1997
and for the Years Ended September 30, 1997 and 1996

	Nine Months Ended June 30,		Years Ended September 30,	
	1998	1997	1997	1996
	(Millions)			
CASH FLOWS FROM OPERATING ACTIVITIES				
Net income (loss)(1)	U.S.$ 87	U.S.$(176)	U.S.$ 8	U.S.$ 61
Items not requiring cash(1)	976	910	1,030	1,125
Other, net	(217)	(38)	28	(276)
Net cash provided by operating activities	846	696	1,066	910
CASH FLOWS FROM INVESTING ACTIVITIES				
Construction expenditures	(401)	(495)	(722)	(1,107)
Allowance for funds used during construction	41	62	81	117
Other, net	(111)	119	61	(264)
Net cash used in investing activities	(471)	(314)	(580)	(1,254)
CASH FLOWS FROM FINANCING ACTIVITIES				
Borrowings, net(2)	(573)	(356)	(352)	637
Other(2)	140	(46)	(73)	(107)
Net cash provided by (used in) financing activities	(433)	(402)	(425)	530
Net change in cash and cash equivalents	U.S.$ (58)	U.S.$ (20)	U.S.$ 61	U.S.$ 186

(1) See Note (1) to Condensed Balance Sheets. The effect on the Condensed Statements of Cash Flows for the nine months ended June 30, 1998 was to decrease Net income by U.S.$54 million and to increase Items not requiring cash by U.S.$54 million.

(2) The nine months ended June 30, 1997 has been reclassified to conform to fiscal 1998 presentation.

Results of Operations for the Nine Months Ended June 30, 1998

Net income for the nine months ended June 30, 1998 amounted to U.S.$87 million, an improvement of U.S.$263 million from the net loss of U.S.$176 million for the same period in fiscal 1997. Operating revenues increased U.S.$484 million from U.S.$3,979 million for the nine months ended June 30, 1997 to U.S.$4,463 million for the nine months ended June 30, 1998. This increase is attributable to a rate increase effective October 1, 1997, as well as an increase in kilowatt-hour sales of 5 percent from 101 billion kilowatt-hours for the nine months ended June 30, 1997 to 106 billion kilowatt-hours for the nine months ended June 30, 1998. The increase in kilowatt-hour sales is primarily attributable to more extreme weather conditions during the nine months ended June 30, 1998 as compared with the same period in fiscal 1997.

Operating expenses for the nine months ended June 30, 1998 were U.S.$2,899 million compared with U.S.$2,646 million for the same period in fiscal 1997. The U.S.$253 million increase consists primarily of higher net fuel and purchased power expense related to higher overall generation, higher coal prices as a result of rail delivery problems, higher depreciation and amortization expenses related to capital project completions, and higher operating and maintenance costs.

Net interest expense decreased U.S.$30 million for the nine months ended June 30, 1998 compared with the same period of fiscal 1997. This interest expense reduction results from lower average interest rates and a lower level of total outstanding debt during fiscal 1998.

Liquidity and Capital Resources

In March 1998, TVA issued in the public market U.S.$1,000 million in Global Power Bonds (due 2013) (the "1998 Series C Bonds") to retire existing debt.

In June 1998, TVA issued in the public market U.S.$575 million in Power Bonds (due 2028) to retire existing debt. For the two months ended August 31, 1998, TVA increased short-term debt owed to the U.S. Treasury by U.S.$127 million.

In September 1998, TVA issued in the public market U.S.$300 million in Power Bonds (due 2001) to retire existing debt, as well as an additional U.S.$500 million of its 1998 Series C Bonds in a second installment to retire existing debt.

In October 1998, TVA issued in the public market U.S.$250 million in Power Bonds (due 2001) to retire existing debt.

Net cash provided by operations increased U.S.$150 million for the nine months ended June 30, 1998, compared with the same period of fiscal 1997. Cash used for construction activities declined U.S.$94 million for the nine months ended June 30, 1998, compared with the same period of fiscal 1997. TVA's total short-term and long-term debt outstanding declined U.S.$567 million during the nine months ended June 30, 1998.

Year 2000 Readiness Disclosure

The "Year 2000 issue" concerns the inability of information technology resources to properly recognize and process date-sensitive information related to the year 2000 and beyond. Because TVA's operations are extensively computerized and are also dependent upon the systems of others with which it conducts business, the failure by TVA or others with which it conducts business to become Year 2000 compliant on a timely basis could have a significant adverse effect on, among other things, TVA's results of operations, liquidity and financial condition as well as TVA's generation and transmission operations. Specific risks to TVA associated with the Year 2000 issue include, but are not limited to, power production and delivery interruptions and administrative and accounting systems malfunctions.

TVA is taking measures to address the impact of the Year 2000 issue on its information technology systems and other systems that may be affected by the Year 2000 issue. TVA's Year 2000 efforts have focused on the following six areas: (1) computer hardware and equipment, (2) application software, (3) systems software, (4) embedded controls, (5) facilities and (6) telecommunications. TVA's Year 2000 efforts with respect to each of these areas consist of five phases: (1) developing a Year 2000 remediation strategy, (2) inventorying and assessing the priority of items that may be affected by the Year 2000 issue, (3) replacing, repairing or converting items affected by the Year 2000 issue, (4) testing and validating the Year 2000 readiness of replaced, repaired and converted items and (5) implementing the replaced, repaired and converted items.

TVA has developed a Year 2000 remediation strategy and has completed both its initial inventory and the majority of its assessments of mission-critical items in each of the six areas described above. In addition, TVA has begun its remediation, testing and implementation of mission-critical items in each of these areas. As of September 30, 1998, TVA's remediation, testing and implementation activities with respect to mission-critical computer hardware and equipment, application software, systems software, facilities and telecommunication systems were approximately 80 percent, 30 percent, 90 percent, 95 percent and 42 percent complete, respectively. TVA expects to complete its remediation, testing and implementation activities in each of these areas by March 1999 except for certain activities that are scheduled to be completed throughout 1999 to minimize disruption of operations.

With respect to embedded controls, TVA's remediation, testing and implementation activities have focused on controls that affect the following four areas: (1) nuclear operations, (2) fossil operations, (3) hydro operations and (4) transmission and power supply operations. As of September 30, 1998, remediation, testing and implementation activities for embedded controls critical to TVA's nuclear, fossil, hydro, and transmission and power supply operations were approximately 10 percent, 15 percent, 60 percent and 25 percent complete, respectively, and are expected to be completed by July 1999, November 1999, January 1999 and May 1999, respectively.

The U.S. Nuclear Regulatory Commission (the "NRC") has notified all utilities operating nuclear power plants that they are required to inform the NRC of steps they are taking to ensure that their computer systems will function properly by the year 2000. In connection therewith, the NRC required each such utility to submit a written indication of, among other things, whether it is pursuing a plan to solve its Year 2000 problems, similar to the plan outlined in the publication *Nuclear Utility Year 2000 Readiness* (the "NEI/NUSMG Plan"). In addition, not later than July 1, 1999, each such utility must submit a written response confirming that its plants are Year 2000 ready, or if its plants are not ready, the utility must provide a status report of work remaining to be done. TVA submitted its required response on July 22, 1998, indicating that it has pursued and is continuing a Year 2000 readiness program similar to that recommended in the NEI/NUSMG Plan.

In addition to remedying its own Year 2000 issues, TVA has been communicating with suppliers, distributors, financial institutions and others with which it does business in an effort to assess the Year 2000 efforts of such entities and to share what TVA is doing to address its Year 2000 issues. As of September 30, 1998, TVA's assessment of the Year 2000 efforts of entities whose Year 2000 readiness is critical to TVA's operations was approximately 48 percent complete, and TVA expects to complete its assessment by June 30, 1999. Although TVA expresses no views about the adequacy of the Year 2000 conversion programs of the suppliers, distributors, financial institutions and other entities with which TVA interfaces, TVA will take the results of these assessments into account in developing its Year 2000 contingency plans.

TVA is in the early stages of developing contingency plans to address system failures that may result from Year 2000 problems. In addition, consistent with the General Accounting Office document *Year 2000 Computing Crisis: Business Continuity and Contingency Planning,* TVA has developed a business partnership program that includes elements for business continuity and contingency planning.

Although it is difficult to give an accurate estimate of the cost of TVA's Year 2000 work, TVA believes that it is allocating sufficient resources to address the Year 2000 issue and does not expect that such costs will be material to TVA's financial position and operations. The projected direct and indirect costs of TVA's Year 2000 work are estimated to be approximately U.S.$38 million, of which approximately U.S.$18 million had already been expended as of September 30, 1998.

Other Matters

In the spring of 1998, TVA's Allen Fossil Plant team received the Rochester Institute of Technology/*USA Today* Quality Cup award in the government category for their work in reducing the cost of compliance with environmental rules requiring coal plants to emit less sulfur dioxide. The team's work resulted in (1) a drop in sulfur dioxide emissions from 80,000 tons annually to 26,000 tons annually, (2) an 80 percent drop in losses from shutdowns of Allen Fossil Plant in fiscal 1997 and (3) U.S.$3 million in savings during fiscal 1997 from switching to low-sulfur coal. The team's plan is being adopted by TVA at other fossil fuel plants.

On April 24, 1998, the TVA Board consolidated TVA's power production, transmission and resource stewardship functions as part of TVA's continuing actions to prepare for success in the restructured utility industry. The TVA Board named Ike Zeringue, previously TVA's Chief Nuclear Officer, to head the functions as President and Chief Operating Officer. John Scalice, formerly TVA's Senior Vice President of Nuclear Operations, served as TVA's acting Chief Nuclear Officer until June 1998, at which time he was named Chief Nuclear Officer & Executive Vice President. TVA believes that consolidating these functions will allow TVA to serve the Tennessee Valley and the nation better in a competitive market. The TVA Board also consolidated TVA's financial functions under the Chief Financial Officer, David N. Smith.

In July 1998, the TVA Board named Claude C. Cross, a veteran of the nuclear Navy and a former senior-level executive with the Institute of Nuclear Power Operations, as its Nuclear Advisor. The Nuclear Advisor provides advice and consultation to the Board about nuclear operations, as needed. In August 1998, Joseph W. Dickey, Executive Vice President, Fossil and Hydro Power Group, resigned. After Dickey's resignation, Joseph R. Bynum, previously Vice President of Fossil Operations, became the Acting Executive Vice President, Fossil and Hydro Power Group.

On March 6, 1998, the GAO released a report discussing federal power marketing administrations. Although this report was not focused on TVA, an appendix to the report repeats comments regarding TVA's competitive position that the GAO initially made in reports released in August 1995 and September 1997. For a discussion of these two reports, see "Competition" in the current Information Statement.

On March 31, 1998, the GAO released a report entitled "Tennessee Valley Authority: Information on Nonpower Programs". The report, which was requested by Senators Fred Thompson and Bill Frist of Tennessee, analyzes TVA's various nonpower activities and compares them to those performed by four investor-owned utilities ("IOUs") around the country. The GAO report concludes that (1) the selected IOUs do not have nonpower roles and responsibilities that are as comprehensive in nature as TVA's; (2) activities such as flood control and navigation tend to be viewed by TVA, the selected IOUs and other officials as the responsibility of the federal government; (3) TVA's land management responsibilities, especially with regard to the Land Between The Lakes, exceed the selected IOUs' land management activities; and (4) the selected IOUs have some programs, such as ones for dam safety, that are similar to nonpower programs operated by TVA.

On March 25, 1998, the Clinton administration proposed a Comprehensive Electricity Competition Plan (the "Plan"), which addresses various aspects of national retail competition in the electric power industry, including extension of the U.S. Federal Energy Regulatory Commission's ("FERC") general regulatory authority to cover transmission service by cooperatives and all government-owned electric systems, including TVA. In addition, the Plan notes that the Clinton administration is considering issues relating to the role that the TVA power system should play in the electric power industry after nationwide competition has begun. The Plan further notes that the administration expects the recommendations of the Tennessee Valley Electric System Advisory Committee (the "Advisory Committee") regarding TVA to provide the administration with a broad framework for bringing competition to TVA and restructuring its operations. The Advisory Committee is a subcommittee of the Secretary of Energy's Advisory Board and includes representatives of TVA, TVA employees, TVA customers, TVA Watch, power marketers and various interest groups in the Tennessee Valley.

Shortly after the release of the Plan, the Advisory Committee released its recommendations regarding TVA. The Advisory Committee members agreed, among other things, that (1) TVA should be subject to FERC transmission jurisdiction comparable to that imposed on other transmitting utilities; (2) TVA should, to some extent, be subject to federal antitrust laws; (3) distributors or their customers should pay some type of excise tax in place of taxes on gross receipts or "in lieu of tax" payments by producers; (4) TVA should relinquish its role of regulating retail power sales; (5) the anti-cherry picking provision and the fence (as both terms are defined in the "Competition" section of the current Information Statement) should be removed concurrently with the implementation of retail competition; (6) TVA should remain primarily a wholesaler of electricity; and (7) any stranded costs resulting from mandated competition should be borne by the customers of TVA or its distributors for whom TVA incurred the costs, subject to review by FERC or another federal authority. The Advisory Committee members did not agree on numerous other issues such as (1) the conditions under which TVA should become subject to FERC transmission jurisdiction; (2) TVA's ability to set its wholesale rates; (3) the extent to which TVA should be subject to federal antitrust laws, labor laws, and income tax; (4) the identity of the entity or entities responsible for regulating retail rates; (5) the nature of TVA's mission; (6) the authority of TVA to build new generation capacity; (7) the extent to which the anti-cherry picking provision and the fence should be removed if retail competition is delayed; (8) the terms of

TVA's wholesale power contracts; (9) the extent to which TVA should be able to serve retail customers; and (10) certain other issues regarding the status and powers of TVA.

A June 23, 1998, draft bill prepared by the House Commerce Committee staff for Representatives Largent and Paxon has many provisions that parallel those to which members of the Advisory Committee agreed in principal. Nevertheless, the Largent draft differs significantly in several respects by providing that (1) sales of power outside the fence could be made only under limited conditions; (2) new generating resources greater than 50 megawatts could be acquired by TVA only if the customers for whose benefit the resources are acquired contractually or financially commit to paying the full cost of the resources; (3) significant transmission investments would require FERC approval; (4) the recovery of stranded costs would be based on FERC's lost-revenue methodology rather than on the competitive-rate methodology, on which the TVA Ten-Year Business Plan is premised; and (5) FERC would be provided broad additional authority to issue regulations and orders related to the management and operation of the TVA power system. Although Congress has not enacted retail choice legislation during 1998, TVA expects that retail electric competition bills will continue to be introduced in the next session of Congress and will receive considerable attention. See "Competition" in the current Information Statement.

In October 1998, Congress appropriated U.S.$50 million for TVA's nonpower programs for fiscal 1999. See "The Basic Resolution; Power Bonds, Discount Notes and Other Indebtedness" — "Recent Legislation" in the current Information Statement. Additionally, Congress enacted legislation permitting TVA to repurchase all of its outstanding U.S.$3.2 billion Power Bonds issued to the Federal Financing Bank (the "FFB") by paying the principal amount of such bonds plus accrued interest to the date of repurchase without making any further payment. The legislation requires TVA to apply a certain portion of the interest savings from the repurchase of its FFB Power Bonds to debt reduction. Pursuant to this legislation, TVA repurchased all of its outstanding Power Bonds issued to the FFB using funds obtained from short-term borrowings. TVA has not issued Power Bonds to the FFB since 1991, and TVA is now prohibited, by the above legislation, from obtaining financing from the FFB.

With the expiration of parts of the collective bargaining agreement between TVA and the Tennessee Valley Trades and Labor Council (the "Council") on December 31, 1997, TVA exercised its right to give a 90-day notice to reopen the remainder of the agreement with the Council and potentially to cancel the agreement. In April 1998, negotiations pursuant to this reopener ended in impasse. To date, TVA has not exercised its right to cancel the agreement, and there is a pending lawsuit by the Council against TVA in which the Council claims that TVA cannot cancel the agreement at this time. In addition, TVA has notified the Council that a dispute exists concerning the employees who constitute an appropriate bargaining unit. Following a hearing on this matter, TVA recently issued a decision finding that one bargaining unit is appropriate for its power organizations and that another bargaining unit is appropriate for trades and labor work within two other organizations. These two units would replace the six separate bargaining units which represent trades and labor employees covered by the TVA-Council agreement. The Council's position is that there is no bargaining unit dispute. Under the collective bargaining agreement, bargaining unit disputes may be appealed to arbitration. See "Employees" in the current Information Statement.

Negotiations from late 1997 through July 1998 resulted in new contractual arrangements with each of the four remaining unions representing TVA white-collar employees. See "Employees" in the current Information Statement.

TVA submitted a proposal to the U.S. Department of Energy ("DOE") to complete Bellefonte as a nuclear plant and to operate it to produce tritium for DOE in addition to electricity. See "Nuclear Power Program" in the current Information Statement. In this proposal, Unit One of Watts Bar Nuclear Plant could be used as a backup to Bellefonte, if necessary. TVA's second proposal to DOE to provide irradiation services to produce tritium at only Unit One of the Watts Bar Nuclear Plant has expired.

In June 1998, following a reevaluation of the likelihood of recovery and the cost of proceeding, TVA withdrew its U.S.$54 million stranded cost claim against Bristol, Virginia. This withdrawal has no impact on TVA's contracts with the 159 distributors of TVA power, all of which have long-term contracts with TVA. See "Competition" in the current Information Statement.

In late September 1998, the Environmental Protection Agency ("EPA") finalized a rule requiring revisions to State Implementation Plans for nitrogen oxide reductions. The rule requires states to submit amendments to their plans to EPA for its review and approval by September 24, 1999. TVA has developed and is implementing a plan to reduce nitrogen oxide emissions at its coal-fired plants by 168,000 tons per year by 2003. Under this plan, TVA will install selective catalytic reduction systems at a number of its coal-fired plants. This plan is consistent with the type of controls that would be needed to comply with EPA's new requirements, though the strategy will not by itself bring TVA into compliance with expected revisions to the state plans. The existing TVA strategy is expected to cost between U.S.$500 million and U.S.$600 million, in addition to amounts TVA has already incurred to comply with the 1990 Clean Air Act Amendments. See "Environmental Matters" in the current Information Statement.

TVA has proposed installing additional natural gas combustion turbines at one or more of its fossil plants by 2000 to help meet increasing demand for electricity during peak periods. The new turbines would produce 500 to 700 megawatts of electricity to augment TVA's current power generation.

In August 1998, the GAO began a study of the TVA Ten-Year Business Plan at the request of two members of Congress. Included within the study are the assumptions that underlie the plan, measurement and estimating methodologies, and specific TVA plans for implementation.

DESCRIPTION OF BONDS

General

The Bonds are to be issued pursuant to authority vested in TVA by the Act and pursuant to the Basic Tennessee Valley Authority Power Bond Resolution adopted on October 6, 1960, as amended on September 28, 1976, October 17, 1989 and March 25, 1992 (the "Basic Resolution"), and the Supplemental Resolution authorizing the Bonds adopted on October 30, 1998 (the "Supplemental Resolution" and together with the Basic Resolution, the "Resolutions"). TVA has entered into a Fiscal Agency Agreement dated as of October 7, 1997 (the "Fiscal Agency Agreement") with the U.S. Federal Reserve Banks, as fiscal agents (together, the "Fiscal Agent"). The U.S. Secretary of the Treasury has approved the time of issuance of, and the maximum rate of interest to be borne by, the Bonds in compliance with Section 15d(c) of the Act. The Bonds represent obligations of TVA payable solely from TVA's Net Power Proceeds and are not obligations of, or guaranteed by, the United States of America.

The Act authorizes TVA to issue and sell bonds, notes and other evidences of indebtedness (hereinafter collectively referred to as "Evidences of Indebtedness") to assist in financing its power program and to refund such Evidences of Indebtedness. Evidences of Indebtedness issued pursuant to Section 2.2 of the Basic Resolution designated as Tennessee Valley Authority Power Bonds are herein referred to as "Power Bonds". The aggregate amount of Evidences of Indebtedness at any one time outstanding is limited to U.S.$30 billion. As of September 30, 1998, TVA had approximately U.S.$25.7 billion and DM 1.5 billion (issued in September 1996) of Evidences of Indebtedness outstanding. At the time TVA issued such DM Evidences of Indebtedness, TVA entered into a currency swap agreement to hedge against fluctuations in such currency. For information with respect to TVA's Power Bonds and the Basic Resolution, see "The Basic Resolution; Power Bonds, Discount Notes and Other Indebtedness" — "Issuance of Additional Bonds and Other Evidences of Indebtedness" in the current Information Statement.

The summaries herein of certain provisions of the Act, the Resolutions and the Fiscal Agency Agreement do not purport to be complete and are qualified in their entirety by reference to all the provisions of the Act, the Resolutions and the Fiscal Agency Agreement, copies of which may be obtained upon written request directed to Tennessee Valley Authority, 400 West Summit Hill Drive, Knoxville, Tennessee 37902, Attention: Vice President and Treasurer, or by calling (423) 632-3366 in the United States.

The Bonds will be Power Bonds as defined above and will be payable as to both principal and interest solely from TVA's Net Power Proceeds, which are defined as the remainder of TVA's Gross Power Revenues (as defined in the Basic Resolution) after deducting the costs of operating, maintaining and administering its power properties (including multiple-purpose properties in the proportion that multiple-purpose costs are allocated to power) and payments to states and counties in lieu of taxes, but before deducting depreciation accruals or other charges representing the amortization of capital expenditures, plus the net proceeds of the sale or other disposition of any Power Facility (as defined in the Basic Resolution) or interest therein. The Act also requires TVA to make certain payments to the U.S. Treasury each year from Net Power Proceeds in excess of those required for debt service as a return on and reduction of the Appropriation Investment (as defined in the Basic Resolution). See "Certain Provisions of the Tennessee Valley Authority Act" — "Payments to the Treasury" in the current Information Statement.

The Bonds rank equally as to the application of Net Power Proceeds with all other Power Bonds. As to the application of Net Power Proceeds, Power Bonds currently rank senior to other Evidences of Indebtedness as to principal and on parity with or senior to other Evidences of Indebtedness as to interest. At some future date prior to maturity of the Bonds, Evidences of Indebtedness other than Power Bonds may also rank on parity with Bonds as to principal. See "The Basic Resolution; Power Bonds, Discount Notes and Other Indebtedness" — "Amendments to the Basic Resolution to Become Effective in the Future" in the current Information Statement. For a further discussion of the application of Net Power Proceeds, see "Certain Provisions of the Tennessee Valley Authority Act" and "The Basic Resolution; Power Bonds, Discount Notes and Other Indebtedness" — "Application of Net Power Proceeds" in the current Information Statement.

There is no limit on other indebtedness or securities which may be issued by TVA and no financial or similar restrictions on TVA, except as provided under the Act, the Basic Resolution and the Supplemental Resolution. TVA issues its Discount Notes pursuant to Section 15d of the Act and in accordance with Section 2.5 of the Basic Resolution. TVA may also issue Other Indebtedness in addition to Power Bonds and Discount Notes. Other Indebtedness, such as TVA's Quarterly Income Debt Securities, are issued pursuant to Section 15d of the Act and under appropriate authorizing resolutions. See "The Basic Resolution; Power Bonds, Discount Notes and Other Indebtedness" in the current Information Statement.

Under the Supplemental Resolution, actions taken by TVA pursuant to U.S. Public Law No. 105-62 shall not be considered an event of default or a breach under the Resolutions. Public Law No. 105-62 provides, among other things, that TVA is required, beginning October 1, 1998, to fund nonpower programs that constitute "essential stewardship activities" with revenues derived from one or more of various sources, including power revenues, notwithstanding provisions of the Act and power bond covenants to the contrary. See the discussion of Public Law 105-62 in "The Basic Resolution; Power Bonds, Discount Notes and Other Indebtedness" — "Recent Legislation" in the current Information Statement.

Possible Future Issuances

The Supplemental Resolution provides that, at the option of TVA, additional Bonds may be issued in one or more future installments pursuant to an amendment to the Supplemental Resolution not requiring the consent of Holders (as such term is defined under "Book-Entry System") of the Bonds. Additional Bonds so issued shall be identical in all respects to the Bonds offered hereby (with any related changes in the issue date, issue price and interest commencement date).

Payment of Principal and Interest

The Bonds will consist of U.S.$2,000,000,000 aggregate principal amount of 5⅜% Global Power Bonds 1998 Series G Due November 13, 2008 (the maturity date being hereinafter referred to as the "Maturity Date"). The Bonds will be issued in minimum denominations of U.S.$1,000 and integral multiples thereof in book-entry form only through the U.S. Federal Reserve Banks as described below under "Book-Entry System". Interest will be payable semiannually in arrear on May 13 and November 13 (each an "Interest Payment Date"), commencing May 13, 1999. Such interest payments will include any interest accrued from and including November 13, 1998 or the preceding Interest Payment Date, as the case may be, to but excluding the relevant Interest Payment Date. Interest shall be computed on the basis of a 360-day year of twelve 30-day months. The Bonds will be repaid at 100% of the principal amount thereof, together with the interest accrued and unpaid thereon, on the Maturity Date. Payments of principal and interest on the Bonds will be made on the applicable payment dates to Holders of the Bonds which are Holders as of the close of business on the Business Day preceding such payment dates, by credit of the payment amount to the Holders' accounts at the U.S. Federal Reserve Banks. The Holder and each other financial intermediary in the chain to the beneficial owner will have the responsibility of remitting payments for the accounts of their customers.

In any case in which an Interest Payment Date or the Maturity Date is not a Business Day, payment of principal or interest, as the case may be, by TVA to the Holders shall be made on the next succeeding Business Day with the same force and effect as if made on such Interest Payment Date or the Maturity Date. The term "Business Day" shall mean any day other than a Saturday or Sunday or a day on which banking institutions in New York City are authorized or required by law or executive order to be closed.

Certain certification requirements are applicable to payments of interest on the Bonds and Strips. The Holder or other persons otherwise required to withhold tax may require the beneficial owner of a Bond or Strip, as a condition of payment of amounts due with respect to such Bond or Strip, to present on a timely basis an appropriate United States Internal Revenue Service Form W-8 (or successor form) or other appropriate form to enable such person to determine its duties and liabilities with respect to any taxes or other charges that may be required to be deducted or withheld under U.S. law or any reporting or other requirements thereunder. See "United States Tax Matters". In the event that any withholding or other tax or information reporting requirements should be imposed by any jurisdiction, TVA has no obligation to pay additional interest or other amounts as a consequence thereof or to redeem the Bonds prior to their stated maturity.

Redemption

The Bonds will not be subject to redemption prior to maturity.

Book-Entry System

The Bonds will be issued and maintained and may be transferred only on the book-entry system of the U.S. Federal Reserve Banks in minimum principal amounts of U.S.$1,000 and additional integral multiples thereof. The U.S. Federal Reserve Banks will maintain book-entry accounts with respect to the Bonds and will make payments, on behalf of TVA, of interest on and principal of the Bonds on the applicable payment dates by crediting Holders' accounts at the U.S. Federal Reserve Banks. The Bonds will not be exchangeable for definitive securities.

The foregoing paragraph is a summary of certain provisions of the Fiscal Agency Agreement and does not purport to be a complete statement of all the provisions of such agreement.

Regulations governing the use of the book-entry system for the Bonds are contained in 18 C.F.R. Part 1314. These regulations and procedures relate primarily to the registration, transfer, exchange and pledge of such obligations. The accounts of Holders on the U.S. Federal Reserve Banks book-entry system are governed by applicable operating circulars of the U.S. Federal Reserve Banks. The U.S. Federal Reserve Banks' handling of, and rights, duties and obligations with respect to, the Bonds will be governed exclusively by the applicable operating circulars of the U.S. Federal Reserve Banks, TVA's book-entry regulations and such other Federal book-entry regulations as may be applicable, notwithstanding any inconsistent procedures or requirements of any depository or organized exchange.

The Bonds may be held of record only by entities eligible to maintain book-entry accounts with the U.S. Federal Reserve Banks. Such entities whose names appear on the book-entry records of a U.S. Federal Reserve Bank as the entities for whose accounts the Bonds have been deposited are herein referred to as "Holders". A Holder is not necessarily the beneficial owner of a Bond. Beneficial owners will ordinarily hold Bonds through one or more financial intermediaries, such as banks, brokerage firms and securities clearing organizations. A Holder that is not the beneficial owner of a Bond, and each other financial intermediary in the chain to the beneficial owner, will have the responsibility of establishing and maintaining accounts for their respective customers. The rights of the beneficial owner of a Bond with respect to TVA and the U.S. Federal Reserve Banks may be exercised only through the Holder thereof. TVA and the U.S. Federal Reserve Banks will have no direct obligation to a beneficial owner of a Bond that is not also the Holder of such Bond. The U.S. Federal Reserve Banks will act only upon the instructions of Holders in recording transfers of the Bonds. See "Clearance and Settlement" with respect to entities holding Bonds through the international clearance and settlement systems.

Stripping

At the request of a Holder, a Bond may be separated ("stripped") into its Interest and Principal Components and maintained as such on the book-entry records of the U.S. Federal Reserve Banks. The components of each stripped Bond are: each future interest payment (each an "Interest Component") and the principal payment (the "Principal Component"). Each Interest Component and the Principal Component will have an identifying designation and CUSIP number as listed in the "Summary of Offering" above.

A Bond may be separated into its Interest and Principal Components at any time from the issue date to but not including November 13, 2008 at the option of the Holder. A request for separation must be made to the Federal Reserve Bank of New York ("FRBNY"). Currently the FRBNY does not charge a fee for such services. Requests for separation from Euromarket participants must be directed through Euroclear or Cedel Bank to the FRBNY. Any applicable requirements of the FRBNY governing stripping must be complied with by the Holder. See "Clearance and Settlement" — "The Clearing Systems".

For a Bond to be stripped into its Interest and Principal Components as described above, the minimum principal amount of the Bond must be U.S.$1,600,000 or integral multiples thereof. This minimum principal amount is the amount, based on the stated interest rate of the Bonds, that will produce a semiannual interest payment of U.S.$1,000 or integral multiples thereof. Interest and Principal Components will be obligations of TVA payable solely from TVA's Net Power Proceeds.

Once a Bond has been stripped into its Interest and Principal Components, the Interest and Principal Components may be maintained and transferred on the book-entry system of the U.S. Federal Reserve Banks in integral multiples of U.S.$1,000. Payments on the Interest and Principal Components will be made on the applicable payment dates on the related Bonds by crediting Holders' accounts at the FRBNY. At the request of a Holder and on the Holder's payment of a fee (currently the FRBNY's fee applicable to on-line book-entry securities transfers), the FRBNY will restore ("reconstitute") the unmatured Interest and Principal Components of a stripped Bond to their fully constituted form. Holders wishing to reconstitute the unmatured Interest and Principal Components of a stripped Bond to their fully constituted form must (i) produce all outstanding Interest and Principal Components for a Bond and (ii) comply with all applicable requirements of the FRBNY governing the stripping and reconstitution of securities. Only stripped Bonds with a minimum original principal amount of U.S.$1,600,000 or integral multiples thereof may be reconstituted. Reconstitution requests from Euromarket participants must be directed through Euroclear or Cedel Bank to the FRBNY.

The selling prices of the Interest and Principal Components could be at substantial discounts from their face amounts and, as a result, these components may be subject to greater interest rate volatility than the fully constituted Bonds or other obligations bearing current interest. There also may be a less liquid secondary market for such Interest and Principal Components as compared to the secondary market for the fully constituted Bonds.

Agents

TVA has agreed, in each case subject to applicable laws and regulations and the provisions of the Fiscal Agency Agreement, the Bonds and the Resolutions, so long as the Bonds are outstanding, to maintain a Fiscal Agent and, so long as the Bonds are listed on the Luxembourg Stock Exchange, a Special Agent in Luxembourg, which will act as an intermediary between TVA and investors in the Bonds. The Fiscal Agent will be the U.S. Federal Reserve Banks. The Special Agent initially will be Kredietbank S.A. Luxembourgeoise. TVA and the Fiscal Agent may amend, modify or supplement, in any respect, or may terminate, substitute or replace, the Fiscal Agency Agreement without the consent of any Holder. In acting under the Fiscal Agency Agreement, the Fiscal Agent acts solely as a fiscal agent of TVA and does not assume any obligation or relationship of agency or trust for or with any Holder of the Bonds except as set forth in applicable operating circulars and letters of the U.S. Federal Reserve Banks. The addresses of the Fiscal Agent and the Special Agent for the Bonds are set forth on the back cover page hereof.

Governing Law

The Fiscal Agency Agreement and the Bonds shall be governed by and construed in accordance with the laws of the State of New York, to the extent such law is not inconsistent with U.S. federal law.

Listings

Application has been made to list the Bonds on the Luxembourg Stock Exchange, the Hong Kong Stock Exchange, the Singapore Stock Exchange and the New York Stock Exchange. Application also has been made to list the Strips on the Luxembourg Stock Exchange.

Notices

Notices and other communications will be given by transmission to a Holder through the communication system linking the U.S. Federal Reserve Banks. Notices will be deemed to have been sufficiently given or made, for all purposes, upon such transmission.

Copies of notices by TVA regarding the Bonds will also be published (a) in a leading daily newspaper in the English language and of general circulation in New York, (b) in a leading daily newspaper in the English language and of general circulation in London, (c) so long as the Bonds are listed on the Luxembourg Stock Exchange and the rules of such Stock Exchange require, in a leading daily newspaper of general circulation in Luxembourg, (d) so long as the Bonds are listed on the Hong Kong Stock Exchange and such Stock Exchange requires, in a leading daily newspaper of general circulation in Hong Kong and (e) so long as the Bonds are listed on the Singapore Stock Exchange and such Stock Exchange requires, in a leading daily newspaper in the English language of general circulation in Singapore. It is expected that copies of such notices will normally be published in *The Wall Street Journal* in New York, *The Financial Times* in London, the *Luxemburger Wort* in Luxembourg, the *South China Morning Post* in Hong Kong and the *Business Times* in Singapore.

CLEARANCE AND SETTLEMENT

The Clearing Systems

Euroclear

The Euroclear System ("Euroclear") is operated by Morgan Guaranty Trust Company of New York, Brussels office. Euroclear holds securities for participating organizations and facilitates multicurrency clearance and settlement of securities transactions between its and Cedel Bank's accountholders through electronic book-entry changes in accounts of its accountholders.

Cedel Bank

Cedel Bank, société anonyme ("Cedel Bank") is incorporated under the laws of Luxembourg as a professional depositary. Cedel Bank holds securities for its participating organizations and facilitates multicurrency clearance and settlement of securities transactions between its and Euroclear's accountholders through electronic book-entry changes in accounts of its accountholders.

Initial Settlement

On initial issue, all Bonds will be issued and settled through the U.S. Federal Reserve Banks book-entry system and held by Holders designated by the Managers. After initial issue, all Bonds will continue to be held by such Holders in the U.S. Federal Reserve Banks book-entry system unless an investor arranges for the transfer of its Bonds to another Holder.

TVA understands that investors electing to hold their Bonds through Euroclear or Cedel Bank accounts will follow the settlement procedures applicable to conventional Eurobonds. Bonds will be credited to the securities clearance accounts of Euroclear and Cedel Bank participants on the business day following the settlement date against payment on the settlement date.

Secondary Market Trading

With respect to secondary market trading in the Bonds, TVA understands the following procedures will apply. Transactions in the Bonds will be cleared and settled by Euromarket participants through the facilities of Euroclear and Cedel Bank, the principal Euromarket securities clearance and settlement organizations. The Bonds may be held of record only by entities eligible to maintain book-entry accounts with the U.S. Federal Reserve Banks. Select entities will hold the Bonds in their book-entry accounts with the FRBNY, as the depositaries for Cedel Bank and Euroclear. The identity of and certain information about the Cedel Bank or Euroclear depositaries may be obtained by contacting Cedel Bank or Euroclear. Transfers of the Bonds between Cedel Bank or Euroclear participants and investors holding directly or indirectly through the U.S. Federal Reserve Banks book-entry system ("Fed Users") will be effected through the book-entry accounts of such depositaries as Holders with the FRBNY, thereby increasing or decreasing their respective holdings of the Bonds on behalf of Cedel Bank or Euroclear.

Transfers between Fed Users will occur in accordance with applicable Book-Entry Regulations promulgated by the U.S. Department of the Treasury. Transfers between Cedel Bank participants and Euroclear participants will occur in the ordinary way in accordance with their applicable rules and operating procedures.

Cross-market transfers between Fed Users, on the one hand, and persons holding Bonds directly or indirectly through Cedel Bank or Euroclear, on the other, will be effected on behalf of the relevant international clearing system by its U.S. depositary; however, such cross-market transactions will require delivery of instructions to the relevant international clearing system by the system participant in accordance with the system's rules and procedures and within its established deadlines (European time). The relevant international clearing system will, if the transaction meets its settlement requirements, deliver instructions to its U.S. depositary to take action to effect final settlement on its behalf by delivering or receiving Bonds through its U.S. Federal Reserve account, and making or receiving payment in accordance with normal procedures for immediately available funds settlement. Instructions of Cedel Bank and Euroclear participants with respect to such transfers must be delivered to Cedel Bank or Euroclear, as the case may be, and not to their U.S. depositaries.

Because of time-zone differences, credits of Bonds received in Cedel Bank or Euroclear as a result of a transaction with a Fed User will be made during the securities settlement processing for the business day following the U.S. Federal Reserve Banks book-entry system settlement date. Such securities credits will be reported to the relevant Cedel Bank or Euroclear participant on such following business day with the cash debt back-valued to, and the interest accruing from, the U.S. Federal Reserve Banks book-entry system settlement date. Cash received in Cedel Bank or Euroclear as a result of sales of Bonds by or through a Cedel Bank participant or a Euroclear participant to a Fed User will be received with value on the U.S. Federal Reserve Banks book-entry system settlement date but will be available in the relevant Cedel Bank or Euroclear cash account only as of the business day following settlement on the U.S. Federal Reserve Banks book-entry system.

From a Fed User's standpoint, a cross-market transaction will settle no differently from a trade between two Fed Users.

Distributions of interest and principal with respect to the Bonds held through Cedel Bank or Euroclear will be credited to the cash accounts of Cedel Bank participants or Euroclear participants on the same day (European time) as payment is made to Fed Users, subject to the relevant system's rules and procedures, to the extent received and applied by its U.S. depositary. Such distributions will be subject to tax reporting in accordance with relevant United States tax laws and regulations. See "United States Tax Matters".

Although Cedel Bank and Euroclear have agreed to the foregoing procedures in order to facilitate transfers of the Bonds among Fed Users, Cedel Bank and Euroclear, they are under no obligation to perform or continue to perform such procedures, and such procedures may be discontinued at any time. None of TVA, the Managers or the Fiscal Agent will have any responsibility for the performance by Euroclear or Cedel Bank or their respective participants or indirect participants of their obligations under the rules and procedures governing their operations.

LEGALITY OF INVESTMENT IN THE UNITED STATES

Each person or entity is advised to consult with its own counsel with respect to the legality of investment in the Bonds or in any stripped Interest and Principal Components thereof (see "Description of Bonds" — "Stripping"), which could be subject to restrictions or requirements with respect to the legality of investment that do not apply to Power Bonds held in their fully constituted form. Generally the following describes the legality of investment in the United States in Power Bonds in their fully constituted form.

Power Bonds are lawful investments and may be accepted as security for all fiduciary, trust and public funds, the investment or deposit of which shall be under the authority or control of any officer or agency of the United States of America. 16 U.S.C. § 831n-4(d).

U.S. national banks may deal in, underwrite and purchase Power Bonds for their own accounts in an amount not to exceed 10% of unimpaired capital and surplus. 12 U.S.C. § 24, seventh paragraph.

U.S. Federal Reserve Banks may accept Power Bonds as eligible collateral for advances to member banks. 12 U.S.C. § 347 and 12 C.F.R. § 201.108(b)(13).

U.S. federal savings associations and U.S. federal savings banks may, to the extent specified in applicable regulations, invest in Power Bonds without regard to limitations generally applicable to investments. 12 U.S.C. § 1464(c)(1)(F).

Power Bonds are eligible as collateral for advances by U.S. Federal Home Loan Banks to members for which Power Bonds are legal investments. 12 U.S.C. § 1430(a) and 12 C.F.R. § 935.9(a)(2).

U.S. federal credit unions may purchase Power Bonds. 12 U.S.C. § 1757(7)(E).

Power Bonds are "obligations of a corporation which is an instrumentality of the United States" within the meaning of Section 7701(a)(19)(C)(ii) of the Internal Revenue Code for purposes of the 60 percent of assets limitation applicable to U.S. building and loan associations.

UNITED STATES TAX MATTERS

Tax Considerations Applicable to Bonds

The following summary of certain United States federal income and estate tax and certain limited state and local tax consequences (where specifically noted) of the purchase, ownership, and disposition of the Bonds has been prepared by Orrick, Herrington & Sutcliffe LLP, as special U.S. tax counsel to TVA, and is based upon laws, regulations, rulings and decisions, which are subject to change at any time, possibly with retroactive effect. The discussion below does not address the tax consequences associated with stripping a Bond into its Interest and Principal Components or of the purchase, ownership, or disposition of an Interest or Principal Component. For a discussion of such tax matters, see "Tax Considerations Applicable to Strips". The discussion does not address all aspects of United States federal income and estate taxation that may be relevant to a particular investor in light of its personal investment circumstances or to certain types of investors subject to special treatment under the United States federal income tax laws (for example, brokers, security dealers, traders in securities that elect to mark to market, banks, life insurance companies, tax-exempt organizations and, with limited exceptions, foreign investors), and generally does not address state and local taxation. Further, the discussion is limited to persons who will hold the Bonds as capital assets and does not deal with United States federal income tax consequences applicable to persons who will hold the Bonds in the ordinary course or as an integral part of their trade or business, or as part of a hedging, straddle, integrated or conversion transaction or persons whose functional currency is not the U.S. dollar. Furthermore, it does not address alternative minimum tax consequences or the indirect effects on the holders of equity interests in a

Bondholder. Each prospective owner of a Bond is urged to consult with its own tax advisor with respect to the United States federal, state and local tax consequences associated with the purchase, ownership, and disposition of a Bond or of an Interest or Principal Component, as well as the tax consequences arising under the laws of any other taxing jurisdiction, and may not construe the following discussion as legal advice.

For purposes of this subsection ("Tax Considerations Applicable to Bonds"), "U.S. Person" means a citizen or resident of the United States, a corporation or (except as may be provided in Treasury Regulations) partnership organized in or under the laws of the United States or any political subdivision thereof, an estate the income of which is includible in gross income for United States tax purposes regardless of its source or a trust if a United States court is able to exercise primary supervision over administration of the trust and one or more U.S. Persons have authority to control all substantial decisions of the trust. The term "U.S. beneficial owner" means a U.S. Person that is a beneficial owner of a Bond.

U.S. Beneficial Owners

A U.S. beneficial owner is subject to federal income taxation on income on a Bond. The Act, however, provides that bonds issued by TVA are "exempt both as to principal and interest from all taxation now or hereafter imposed by any State or local taxing authority except estate, inheritance and gift taxes". This exemption might not extend to franchise or other non-property taxes in lieu thereof imposed on corporations or to gain or loss realized upon the sale or exchange of a Bond, notwithstanding that such gain might in some cases be treated as interest income for United States federal income tax purposes.

Interest on a Bond will be taxable to a U.S. beneficial owner at the time that it is received or accrued, depending upon the U.S. beneficial owner's method of accounting for United States federal income tax purposes. There is no special exemption for a Bond from United States federal income, estate and gift tax.

Upon a sale or exchange of a Bond, a U.S. beneficial owner generally will recognize capital gain or loss equal to the difference between the amount realized on the sale or exchange (not including any amounts attributable to accrued and unpaid interest) and the U.S. beneficial owner's adjusted basis for the Bond for federal income tax purposes.

If a U.S. beneficial owner purchases a Bond for less than its stated redemption price at maturity, in general, that difference will be market discount (unless the discount is less than ¼ of 1% of the stated redemption price at maturity of the Bond multiplied by the number of complete years remaining to maturity). In general, under the market discount rules, unless the U.S. beneficial owner elects to include market discount in income currently, any gain on a disposition of a market discount Bond will be ordinary income to the extent of accrued market discount, and deductions for some or all of the interest on any indebtedness incurred or continued to purchase or carry the Bond may be deferred until the disposition of the Bond. Any election to include market discount in income currently generally applies to all debt instruments acquired by the electing U.S. beneficial owner during or after the first taxable year to which the election applies and is irrevocable without the consent of the United States Internal Revenue Service. A U.S. beneficial owner should consult a tax advisor before making the election.

A U.S. beneficial owner who purchases a Bond for an amount greater than the amount payable at maturity of the Bond may elect to amortize the bond premium. In the case of a U.S. beneficial owner that makes an election to amortize bond premium or has previously made an election that remains in effect, amortizable bond premium on the Bond generally will be treated as a reduction of the interest income on a Bond on a constant yield basis (except to the extent regulations may provide otherwise) over the term of the Bond. The basis of a debt obligation purchased at a premium is reduced by the amount of amortized bond premium. An election to amortize bond premium generally applies to all debt instruments (other than tax-exempt obligations) held by the electing U.S. beneficial owner on the first day of the first taxable year to which the election applies or thereafter acquired by such owner, and is irrevocable without consent of the United States Internal Revenue Service. A U.S. beneficial owner should consult a tax advisor before making the election.

A U.S. beneficial owner may elect to include in gross income all interest that accrues on a debt instrument using the constant yield method described below under the heading "Tax Considerations Applicable to Strips". For purposes of this election, interest includes stated interest, original issue discount ("OID"), market discount, de minimis market discount and unstated interest, as adjusted by any amortizable bond premium or acquisition premium. If this election is made with respect to a debt instrument with amortizable bond premium, the electing U.S. beneficial owner will be deemed to have elected to apply amortizable bond premium against interest with respect to all debt instruments with amortizable bond premium (other than debt instruments the interest on which is excludible from gross income) held by the electing U.S. beneficial owner as of the beginning of the taxable year in which the debt instrument with respect to which the election is made is acquired or thereafter acquired. The deemed election with respect to amortizable bond premium may not be revoked without the consent of the United States Internal Revenue Service. If this election is made with respect to a debt instrument with market discount, the electing U.S. beneficial owner will be deemed to have elected to include market discount in income currently (as discussed above) with respect to all debt instruments acquired by the electing U.S. beneficial owner during or after the first taxable year to which the election applies, which election may not be revoked without the consent of the United States Internal Revenue Service.

Non-U.S. Beneficial Owners

Generally, a Bondholder that is not a U.S. Person and that has no connection with the United States other than holding the Bond (a "non-U.S. beneficial owner") will not be subject to United States federal withholding tax on interest on a Bond. To qualify for the exemption from withholding, the last U.S. Person in the chain of payment prior to payment to a non-U.S. beneficial owner (the "Withholding Agent") must have received in the year in which such a payment occurs, or in either of the two preceding years, a statement that (i) is signed by the beneficial owner under penalties of perjury, (ii) certifies that such owner is not a U.S. beneficial owner and (iii) provides the name and address of the beneficial owner. The statement may be made on a United States Internal Revenue Service Form W-8 or substantially similar substitute form, and the beneficial owner must inform the Withholding Agent of any change in the information on the statement within 30 days of such change. If a Bond is held through a securities clearing organization or certain other financial institutions, the organization or institution may provide a signed statement to the Withholding Agent. However, in such case, the signed statement must be accompanied by a copy of a Form W-8 or substitute form provided by the beneficial owner to the organization or institution holding the Bond on behalf of the beneficial owner.

Recently issued regulations would provide alternative methods for satisfying the certification requirements described above (the "New Regulations"). The New Regulations also would require, in the case of Bonds held by a foreign partnership, that (a) the certification described above be provided by the partners rather than by the foreign partnership and (b) the partnership provide certain information, including a United States taxpayer identification number. A look-through rule would apply in the case of tiered partnerships. The New Regulations are generally effective for payments made after 1999. There can be no assurance that the New Regulations will not be amended prior to the date they first become effective.

Generally, any amount which constitutes capital gain to a non-U.S. beneficial owner upon retirement or disposition of a Bond will not be subject to U.S. federal income taxation in respect of such amount. Certain exceptions may be applicable and individual non-U.S. beneficial owners are particularly urged to consult a tax advisor. Generally, the Bonds will not be includible in the U.S. federal estate of a non-U.S. beneficial owner.

Backup Withholding

Backup withholding of United States federal income tax at a rate of 31% may apply to payments made in respect of the Bonds to beneficial owners who are not exempt recipients and who fail to provide certain identifying information (such as the beneficial owner's taxpayer identification number) in the manner required. Generally, individuals are not exempt recipients, whereas corporations and certain other entities generally are exempt recipients. Payments made in respect of the Bonds to a U.S. beneficial owner must be reported to the United States Internal Revenue Service, unless such U.S. beneficial owner is an exempt recipient or establishes an exemption. Compliance with the identification procedures (described in the preceding section) would generally establish an exemption from backup withholding for those non-U.S. beneficial owners who are not exempt recipients.

In addition, upon the sale of a Bond to (or through) a broker, the broker must withhold at a rate of 31% of the reportable payment, unless either (i) the broker determines that the seller is a corporation or other exempt recipient or (ii) the seller provides, in the required manner, certain identifying information and, in the case of a non-U.S. beneficial owner, certifies that such seller is a non-U.S. beneficial owner (and certain other conditions are met). Such a sale must also be reported by the broker to the United States Internal Revenue Service, unless either (i) the broker determines that the seller is an exempt recipient or (ii) the seller certifies its non-U.S. status (and certain other conditions are met). Certification of the beneficial owner's non-U.S. status usually would be made on Form W-8 under penalties of perjury, although in certain cases it may be possible to submit other documentary evidence. The term "broker" generally includes all persons who, in the ordinary course of a trade or business, stand ready to effect sales made by others, as well as brokers and dealers registered as such under the laws of the United States or a state. These requirements generally will apply to a United States office of a broker, and the information reporting requirements generally will apply to a foreign office of a United States broker, as well as to a foreign office of a foreign broker if the broker is (i) a controlled foreign corporation within the meaning of Section 957(a) of the Internal Revenue Code, (ii) a foreign person 50% or more of whose gross income from all sources for the 3-year period ending with the close of its taxable year preceding the payment (or for such part of the period that the foreign broker has been in existence) was effectively connected with the conduct of a trade or business within the United States or (iii) under the New Regulations (applicable with respect to payments made after 1999), a foreign partnership if it is engaged in a trade or business in the United States or if 50% or more of its income or capital interests are held by U.S. Persons.

Generally, any amounts withheld under the backup withholding rules from a payment to a beneficial owner would be allowed as a refund or credit against such beneficial owner's United States federal income tax.

Tax Considerations Applicable to Strips

The following discussion of the United States federal income and estate tax and certain limited state and local tax consequences (where specifically noted) of the purchase, ownership and disposition of Strips has been prepared by Orrick, Herrington & Sutcliffe LLP, as special U.S. tax counsel to TVA, and is based upon laws, regulations, rulings and decisions, which are subject to change at any time, possibly with retroactive effect. The discussion does not address all aspects of United States federal income and estate taxation that may be relevant to a particular investor in light of its personal investment circumstances or to certain types of investors subject to special treatment under the United States federal income tax laws (for example, brokers, security dealers, traders in securities that elect to mark to market, banks, life insurance companies, tax-exempt organizations and, with limited exceptions, foreign investors), and generally does not address state and local taxation. Further, the discussion is limited to persons who will hold the Strips as capital assets, and does not deal with United States federal income tax consequences applicable to persons who will hold the Strips in the ordinary course or as an integral part of their trade or business, or as part of a hedging, straddle, integrated or conversion transaction or persons whose functional currency is not the U.S. dollar. Furthermore, it does not address alternative minimum tax consequences or the indirect effects on the holders of equity interests in a Bondholder. Each prospective owner of a Strip is urged to consult with its own tax advisor with respect to the United States federal, state and local tax consequences associated with the purchase, ownership and disposition of a Strip, as well as tax consequences arising under the laws of any other taxing jurisdiction, and may not construe the following discussion as legal advice.

For purposes of this subsection ("Tax Considerations Applicable to Strips"), "U.S. Person" means a citizen or resident of the United States, a corporation or (except as may be provided in the Treasury Regulations) a partnership organized in or under the laws of the United States or any political subdivision thereof, an estate or trust the income of which is includible in gross income for United States tax purposes regardless of its source or a trust if a United States court is able to exercise primary supervision over administration of the trust and one or more U.S. Persons have authority to control all substantial decisions of the trust. The term "U.S. beneficial owner" means a U.S. Person that is a beneficial owner of a Strip.

U.S. Beneficial Owners

A U.S. beneficial owner is subject to United States federal income taxation on the income of a Strip, and there is no special exemption from United States federal income, estate and gift tax with respect to Strips. The Act provides that bonds issued by TVA are "exempt both as to principal and interest from all taxation now or hereafter imposed by any State or local taxing authority except estate, inheritance and gift taxes". This exemption might not extend to franchise or other non-property taxes in lieu thereof imposed on corporations or to gain or loss realized upon the sale or exchange of a Bond, notwithstanding that such gain might in some cases be treated as interest income for United States federal income tax purposes. It is unclear whether this exemption applies at all to the income on a Strip. If all of the income on a Strip were to be exempt from state and local taxation, the amount of income exempted from such taxation could be in excess of the amount that would have been exempted had the Bonds not been separated into their Interest and Principal Components. It is unclear whether or not this was intended. Therefore, while it is believed that the income includible by a U.S. beneficial owner with respect to a Strip should qualify for the exemption provided in the Act at least to the extent of the rate of interest payable on the Bonds, there is no controlling precedential authority and, therefore, each owner of a Strip is urged to consult its own tax advisor as to whether or not the income of a Strip qualifies in whole or in part for the exemption provided in the Act.

A U.S. beneficial owner that elects to strip a Bond into its Interest and Principal Components and to dispose of one or more of such Components will be required to include in income all interest and market discount accrued on the Bond to the date of disposition (to the extent that such income has not previously been included in income), and the U.S. beneficial owner's basis in the Bond will be increased, immediately prior to the disposition of one of the Strips, by the amount so included in income. Upon the disposition of a Strip, the U.S. beneficial owner will be required to recognize gain or loss equal to the difference between the amount realized on the disposition of the Strip and the U.S. beneficial owner's basis in the Strip immediately prior to the disposition of one of the Strips. For purposes of determining that basis, the U.S. beneficial owner will be required to allocate its tax basis in the Bond immediately prior to the sale (as adjusted in the manner detailed above) between the Interest and Principal Components based on their respective fair market values on the date of the sale.

A U.S. beneficial owner of a Strip will accrue income on the Strip in accordance with the original issue discount ("OID") rules set forth in the United States Internal Revenue Code of 1986. In this regard, the application of the OID rules to the Strips is subject to significant uncertainty, and therefore purchasers of the Strips are urged to consult with their own tax advisors. Generally, however, it is anticipated that each U.S. beneficial owner of a Strip will be required to include in income, as OID, the difference between (1) the stated redemption price at maturity of the Interest or Principal Component owned by such person (which generally would include all payments to be made on the Component subsequent to the date that the strip was effected or, if later, the date of the U.S. beneficial owner's purchase of the Component) and (2) the U.S. beneficial owner's purchase price for the Component (or, in the case of a person who effects a strip and disposes of one or more of the Components, the portion of the person's basis in the Bond which is allocable to the retained Components, as determined pursuant to the rules set forth in the preceding paragraph).

The amount of OID on a Strip (determined as set forth above) will be includible on a constant-yield basis in the income of a U.S. beneficial owner of a Strip over the life of the Strip (excluding, with respect to certain U.S. beneficial owners, Strips having a maturity of one year or less from the date of purchase — which Strips would be subject to special OID rules which are discussed below), even in years in which the owner of the Strip does not receive any actual payment. The amount of OID that must be included in income each year by the U.S. beneficial owner of a Strip will be equal to the sum of the daily portions of the OID that accrued during each day of the year during which the U.S. beneficial owner owned the Strip. The daily portions will be determined by allocating to each day of the accrual period, as defined below, a pro rata portion of an amount equal to the adjusted issue price of the Strip at the beginning of the accrual period, also as defined below, multiplied by the yield to maturity of the Strip, determined by compounding at the close of each accrual period and properly adjusted for the length of the accrual period. For purposes of these calculations, (i) the accrual periods will, generally, be of any length and may vary in length over the term of the Strip, provided that each accrual period is no longer than a year and that each scheduled payment of principal and interest occurs either on the final day of an accrual period or on the first day of an accrual period, and (ii) the adjusted issue price of a Strip will be the U.S. beneficial owner's purchase price for the Strip (or, in the case of a person who effects a strip and disposes of one or more of the Components, the portion of the person's basis in the Bond which is allocable to the retained Components, as determined pursuant to the rules set forth above), increased by the OID accrued by the U.S. beneficial owner in previous accrual periods and decreased by any payments received by the U.S. beneficial owner in prior accrual periods. The amount of OID allocable to an initial short accrual period may be computed using any reasonable method if all other accrual periods other than a final short accrual period are of equal length. The amount of OID allocable to the final accrual period is the difference between (x) the amount payable at the maturity of the Strip and (y) the Strip's adjusted price as of the beginning of the final accrual period. The foregoing rules will generally be applied by each Strip acquired separately. In certain circumstances, Strips acquired (or retained by the person stripping a Bond) may be treated as a single instrument for tax purposes.

In general, a cash basis U.S. beneficial owner who purchases a Strip the payment with respect to which is due not later than one year from the date of issuance ("short-term Strips") is not required to accrue OID (as determined under the special rule described below for the purposes of this paragraph) for United States federal income tax purposes unless it elects to do so. Accrual basis U.S. beneficial owners and certain other U.S. beneficial owners (including banks, regulated investment companies, dealers in securities, common trust funds, U.S. beneficial owners who hold the debt instruments as part of certain identified hedging transactions, certain pass-through entities and electing cash basis U.S. beneficial owners) who purchase a short-term Strip and any U.S. beneficial owners who strip a Bond into its Interest and Principal Components and who retain one or more such Components are required to accrue OID on short-term Strips on either a straight-line basis or under the constant-yield method (based on daily compounding), at the election of the U.S. beneficial owner. In the case of a U.S. beneficial owner not required and not electing to include OID on a short-term Strip in income currently, any gain realized on the sale or retirement of the short-term Strip will be ordinary income to the extent of the OID accrued on a straight-line basis (unless an election is made to accrue the OID under the constant-yield method) through the date of sale or retirement. U.S. beneficial owners who are not required and who do not elect to accrue OID on short-term Strips will be required to defer deductions for interest on borrowings allocable to short-term Strips in an amount not exceeding the deferred income until the deferred income is realized.

Upon the sale or exchange of a Strip, a U.S. beneficial owner generally will recognize capital gain or loss equal to the difference between the amount realized on the sale or exchange and the U.S. beneficial owner's adjusted tax basis in the Strip. A U.S. beneficial owner's adjusted tax basis in a Strip will generally be its cost, increased by the amount of the OID included in the U.S. beneficial owner's income with respect to the Strip.

TVA is selling the Bonds (and not Strips) to the Managers; it is possible, however, that the Managers may elect to strip the Bonds and sell Interest and Principal Components (as well as Bonds) immediately upon their acceptance of the Bonds. Such Strips might be viewed, for United States federal income tax purposes, as OID bonds issued by TVA to the purchasers of the Strips. If the United States Internal Revenue Service were to characterize the transaction in this fashion, the rules set forth above would generally apply to the Bonds stripped by the Managers, except that (1) the amount of OID on each Strip so sold would be measured, and the adjusted issue price would be determined, by reference to the first price at which a substantial amount of each Strip was sold, rather than by reference to the price paid by the purchaser for the Strip (not only in the case of an initial purchaser of the Strip, but also in the case of any transferee thereof) and (2) the stated redemption price at maturity would be determined by reference to all payments to be made on the Strip subsequent to the date of the closing relating to the Bonds offered hereby rather than by reference to the payments to be made subsequent to the U.S. beneficial owner's acquisition of the Strip. Each U.S. beneficial owner is urged to consult with its own tax advisor as to the likelihood of such a characterization, as well as to the application of the "acquisition premium" and "market discount" rules which would apply to those Bonds stripped by the Managers if the transaction were to be so characterized.

Recombinations. The OID rules are also unclear as to the treatment of a U.S. beneficial owner who acquires a Principal Component and all the associated Interest Components; it is believed, however, that such a person would not treat the Components as a Bond, but would instead recognize income on each of the Components in the manner detailed above. However, if such a person requests the FRBNY to reconstitute the Components into a Bond and that Bond is then sold to another person, it is believed that the new purchaser would be treated as having acquired a Bond (rather than Interest and Principal Components) with the result that the rules set forth above, under "Tax Considerations Applicable to Bonds", would apply. Each purchaser of a Strip is urged to consult its own tax advisor as to this issue.

Non-U.S. Beneficial Owners

In certain circumstances, Strips acquired (or retained by the person stripping a Bond) may be treated as a single instrument for tax purposes. A non-U.S. beneficial owner of a Strip will not be subject to United States federal withholding tax on the income of the Strip. To qualify for the exemption from withholding, the Withholding Agent must have received in the year in which such payment occurs, or in either of the two preceding years, a statement that (i) is signed by the beneficial owner under penalties of perjury, (ii) certifies that such owner is a non-U.S. beneficial owner and (iii) provides the name and address of the beneficial owner. The statement may be made on an United States Internal Revenue Service Form W-8 or substantially similar substitute form, and the beneficial owner must inform the Withholding Agent of any change in the information on the statement within 30 days of such change. If a Strip is held through a securities clearing organization or certain other financial institutions, the organization or institution may provide a signed statement to the Withholding Agent. However, in such case, the signed statement must be accompanied by a Form W-8 or substitute form provided by the beneficial owner to the organization or institution holding the Strip on behalf of the beneficial owner.

The New Regulations would provide alternative methods for satisfying the certification requirements described above. The New Regulations also would require, in the case of Strips held by a foreign partnership, that (a) the certification described above be provided by the partners rather than by the foreign partnership and (b) the partnership provide certain information, including a United States taxpayer identification number. A look-through rule would apply in the case of tiered partnerships. The New Regulations are generally effective for payments made after 1999. There can be no assurance that the New Regulations will not be amended prior to the date they first become effective.

Generally, any amount which constitutes capital gain to a non-U.S. beneficial owner upon retirement or disposition of a Strip will not be subject to United States federal income taxation. Certain exceptions may be applicable and individual non-U.S. beneficial owners are particularly urged to consult their own tax advisors.

Generally, the Strips will not be includible in the U.S. federal estate of a non-U.S. beneficial owner.

Backup Withholding

Backup withholding of United States federal income tax at a rate of 31% may apply to payments made in respect of the Strips to beneficial owners of the Strips that are not "exempt recipients" and that fail to provide certain identifying information (such as taxpayer identification number) to the Withholding Agent at the time and in the manner required. Such backup withholding may also apply in the case of payments made upon the disposition of a Strip. Individuals generally are not exempt recipients, whereas corporations and certain other entities are generally exempt recipients. Compliance with the identification procedures described in the preceding section would generally establish an exemption from backup withholding for those non-U.S. beneficial owners who are not exempt recipients.

In addition, upon the sale of a Strip to (or through) a broker, the broker must withhold at a rate of 31% of the reportable payment, unless either (i) the broker determines that the seller is a corporation or other exempt recipient or (ii) the seller provides, in the required manner, certain identifying information and, in the case of a non-U.S. beneficial owner, certifies that such seller is a non-U.S. beneficial owner (and certain other conditions are met). Such a sale must also be reported by the broker to the Internal Revenue Service, unless either (i) the broker determines that the seller is an exempt recipient or (ii) the seller certifies its non-U.S.

status (and certain other conditions are met). Certification of the beneficial owner's non-U.S. status usually would be made on Form W-8 under penalties of perjury, although in certain cases it may be possible to submit other documentary evidence. The term "broker" generally includes all persons who, in the ordinary course of a trade or business, stand ready to effect sales made by others, as well as brokers and dealers registered as such under the laws of the United States or a state. These requirements generally will apply to a United States office of a broker, and the information reporting requirements generally will apply to a foreign office of a United States broker, as well as to a foreign office of a foreign broker if the broker is (i) a controlled foreign corporation within the meaning of Section 957(a) of the Internal Revenue Code, (ii) a foreign person 50% or more of whose gross income from all sources for the 3-year period ending with the close of its taxable year preceding the payment (or for such part of the period that the foreign broker has been in existence) was effectively connected with the conduct of a trade or business within the United States or (iii) under the New Regulations (applicable with respect to payments made after 1999), a foreign partnership if it is engaged in a trade or business in the United States or if 50% or more of its income or capital interests are held by U.S. Persons.

Generally, any amounts withheld under the backup withholding rules from a payment to a beneficial owner would be allowed as a refund or a credit against such beneficial owner's United States federal income tax.

SUBSCRIPTION AND SELLING

Subject to the terms and conditions set forth in the Subscription Agreement relating to the Bonds, TVA has agreed to sell to each of the Managers named below (the "Managers") and each of the Managers, for which Lehman Brothers International (Europe) and J.P. Morgan Securities Inc. are acting as Lead Managers, has severally agreed to purchase, the principal amount of Bonds set forth opposite its name below:

Manager	Principal Amount
Lehman Brothers International (Europe)	U.S.$ 900,000,000
J.P. Morgan Securities Inc.	900,000,000
Credit Suisse First Boston Corporation	40,000,000
Deutsche Bank AG London	40,000,000
First Tennessee Bank National Association	40,000,000
Goldman, Sachs & Co.	40,000,000
Morgan Stanley & Co. International Limited	40,000,000
Total	U.S.$2,000,000,000

The Subscription Agreement provides that the obligations of the Managers are subject to certain conditions precedent and that the Managers will be obligated to purchase all of the Bonds if any are purchased.

The Managers have advised TVA that they propose to offer all or part of the Bonds directly to the public initially at the offering prices set forth on the cover page of this Offering Circular and to dealers at such prices less a concession not in excess of .200% of the principal amount thereof. The Managers may allow and such dealers may reallow discounts not in excess of .125% of the principal amount of the Bonds to certain other dealers. After the initial offering, the public offering price and concession may be changed.

The Managers immediately upon their acceptance of the Bonds may, but are not obligated to, strip some or all of the Bonds and deliver Interest and/or Principal Components rather than Bonds to investors purchasing Strips. Sales of any such Strips would be at negotiated prices.

Each Manager represents, warrants and agrees to and with TVA that such Manager and its Affiliates (as defined herein) (i) have not offered or sold Bonds and, prior to six months after the Closing Date, will not offer or sell any Bonds to persons in the United Kingdom except to persons whose ordinary activities involve them in acquiring, holding, managing or disposing of investments (as principal or agent) for the purposes of their businesses or otherwise in circumstances which have not resulted and will not result in an offer to the public in the United Kingdom within the meaning of the Public Offers of Securities Regulations 1995; (ii) have complied and will comply with all applicable provisions of the United Kingdom Financial Services Act 1986 with respect to anything done by them in relation to the Bonds in, from or otherwise involving the United Kingdom; and (iii) have only issued or passed on and will only issue or pass on in the United Kingdom any document received by them in connection with an issue of Bonds to a person who is of a kind described in Article 11(3) of the United Kingdom Financial Services Act 1986 (Investment Advertisements) (Exemptions) Order 1996 (as amended) or is a person to whom such document may otherwise lawfully be issued or passed on. The term "Affiliate" means any person that directly, or indirectly through one or more intermediaries, controls, is controlled by, or is under common control with a Manager. For purposes of this definition of Affiliate, the term "control" (including the terms "controlled by" and "under common control with") means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies, including without limitation the investment or trading decisions of a person, whether through ownership of voting securities, by contract or otherwise.

Each Manager represents, warrants and agrees to and with TVA that such Manager and its Affiliates (i) have not offered or sold and will not offer or sell in Hong Kong, by means of any document, any Bonds other than to persons whose ordinary business it is to buy or sell shares or debentures, whether as principal or agent, or in circumstances which do not constitute an offer to the public within the meaning of the Companies

Ordinance (Cap. 32) of Hong Kong, and (ii) unless they are persons who are permitted to do so under the securities laws of Hong Kong, have not issued, or had in their possession for the purposes of issuing, and they will not issue, or have in their possession for the purposes of issue, any advertisement, invitation or document relating to the Bonds other than in respect of Bonds intended to be disposed of to persons outside Hong Kong or to be disposed of in Hong Kong only to persons whose business involves the acquisition, disposal or holding of securities, whether as principal or as agent.

Each Manager acknowledges that the Offering Circular has not been and will not be registered as a prospectus with the Registrar of Companies in Singapore. Accordingly, each Manager represents, warrants and agrees to and with TVA that such Manager and its Affiliates have not offered or sold, and will not offer or sell, any Bonds, nor will they circulate or distribute the Offering Circular or any other offering document or material relating to the Bonds, directly or indirectly, to the public or any member of the public in Singapore other than (i) to an institutional investor or other person specified in Section 106C of the Companies Act, Chapter 50 of Singapore (the "Singapore Companies Act"), (ii) to a sophisticated investor, and in accordance with the conditions, specified in Section 106D of the Singapore Companies Act or (iii) otherwise pursuant to, and in accordance with the conditions of, any other applicable provision of the Singapore Companies Act.

Purchasers of Bonds or Strips may be required to pay stamp taxes and other charges in accordance with the laws and practices of the country of purchase in addition to the issue price set forth above.

All secondary trading in Bonds and Strips will settle in immediately available funds. See "Clearance and Settlement" — "Secondary Market Trading".

TVA has agreed to indemnify the Managers against certain civil liabilities.

GENERAL INFORMATION

1. The issuance of the Bonds was authorized pursuant to the Resolutions. At the date of issue, all necessary legal authorizations for issuance of the Bonds will have been obtained by TVA.

2. The Bonds and Strips have been accepted for clearance by Euroclear and Cedel Bank. The identifying numbers are as set forth on page C-7.

3. There has been no material adverse change in the financial position of TVA since June 30, 1998.

4. There is no litigation, actual or threatened, which relates to TVA and to which TVA is a party or of which TVA has been notified that it will be made a party which is material in the context of the issuance of the Bonds.

5. In connection with the Luxembourg Stock Exchange listing application, copies of the Act, the Resolutions and book-entry regulations of TVA and a legal notice relating to the issuance of the Bonds will be deposited prior to listing with the *Greffier en Chef du Tribunal D'Arrondissement de et à Luxembourg*, where copies thereof may be obtained upon request. Copies of the Act, the Resolutions, the Fiscal Agency Agreement, annual and quarterly financial reports, and Information Statements and supplements thereto of TVA will be available for inspection and may be obtained at the office of the Special Agent, free of charge, as long as the Bonds are listed on the Luxembourg Stock Exchange and at the offices of Allen & Overy, 9th floor, Three Exchange Square, Central, Hong Kong and at the offices of Allen & Gledhill, 36 Robinson Road #18-01, City House, Singapore.

6. TVA has received from PricewaterhouseCoopers LLP, independent accountants and successors to Coopers & Lybrand L.L.P., an acknowledgment dated November 6, 1998, that it agrees to the incorporation by reference in this document of its report dated October 23, 1997, on its audit of the financial statements of TVA at September 30, 1997 and 1996 and for each of the three years in the period ended September 30, 1997, which report is included in TVA's Information Statement, dated February 27, 1998.

VALIDITY OF BONDS

The validity of the Bonds will be passed upon for TVA by Edward S. Christenbury, Esq., General Counsel of TVA, and for the Managers by Sullivan & Cromwell, 1701 Pennsylvania Avenue, N.W., Washington, DC 20006, U.S.A.

* * * * * *

Any statements in this Offering Circular involving matters of opinion, whether or not expressly so stated, are intended as such and not as representations of fact. This Offering Circular is not to be construed as a contract or agreement with the purchaser of any of the Bonds.

TENNESSEE VALLEY AUTHORITY

By: /s/ DAVID N. SMITH

David N. Smith
Chief Financial Officer

Dated November 6, 1998

INFORMATION STATEMENT

TENNESSEE VALLEY AUTHORITY

A Wholly Owned Corporate Agency and Instrumentality of the

UNITED STATES OF AMERICA

The Tennessee Valley Authority ("TVA" or the "Corporation") presents this Information Statement ("Statement") for the information of potential purchasers of its Power Bonds (the "New Power Bonds"), including its First Installment Series Bonds (the "Installment Bonds" — sometimes called "FISBS"), its Discount Notes and such other evidences of indebtedness ("Other Indebtedness") it may issue pursuant to the Act (as defined below). New Power Bonds are to be issued pursuant to authority vested in TVA by the Tennessee Valley Authority Act of 1933, as amended (the "Act"), and the Basic Tennessee Valley Authority Power Bond Resolution adopted by the Board of Directors of TVA (the "Board") on October 6, 1960, as amended on September 28, 1976, October 17, 1989, and March 25, 1992 (the "Basic Resolution"). Discount Notes and Other Indebtedness are issued pursuant to the Act and their respective authorizing resolutions.

TVA may from time to time offer New Power Bonds and Other Indebtedness and may offer on a continuous basis Discount Notes for sale by direct placements or through selected investment dealers, dealer banks, underwriters, or underwriting syndicates as TVA deems appropriate. Information concerning particular offerings of New Power Bonds, Discount Notes or Other Indebtedness will be described in an appropriate offering circular and in any supplement thereto. This Statement, and any supplement hereto, should be read in conjunction with the offering circular and any supplement thereto for the particular New Power Bonds, Discount Notes or Other Indebtedness being offered.

This Statement will be updated by supplements or replaced from time to time to reflect annual financial results of the Corporation and as otherwise determined appropriate by the Corporation. Any provisions herein modified or superseded shall not be deemed, except as so modified, to constitute a part of this Statement. Additional copies of this Statement may be obtained upon written request directed to Tennessee Valley Authority, 400 West Summit Hill Drive, Knoxville, Tennessee 37902, Attention: Vice President and Treasurer, or by calling (423) 632-3366.

No salesperson, dealer or other person has been authorized to give any information or to make any representations not contained herein or in a specific offering circular or supplement approved by TVA, and, if given or made, such information or representation must not be relied upon as having been authorized by TVA. This Statement and any offering circular or supplement do not constitute an offer to sell or a solicitation of any offer to buy any of the New Power Bonds, Discount Notes or Other Indebtedness offered thereby in any jurisdiction to any person to whom it is unlawful to make such offer in such jurisdiction. The delivery of this Statement and any offering circular or supplement at any time does not imply that the information given herein or therein is correct at any time subsequent to its respective date.

THE NEW POWER BONDS, DISCOUNT NOTES, AND OTHER INDEBTEDNESS OF TVA WILL NOT BE OBLIGATIONS OF, NOR WILL PAYMENT OF PRINCIPAL THEREOF OR ANY INTEREST THEREON BE GUARANTEED BY, THE UNITED STATES OF AMERICA. PRINCIPAL AND INTEREST, IF ANY, WILL BE PAYABLE SOLELY FROM TVA'S NET POWER PROCEEDS AS HEREIN DEFINED. THE NEW POWER BONDS, DISCOUNT NOTES, AND OTHER INDEBTEDNESS ARE NOT REQUIRED TO BE REGISTERED UNDER THE SECURITIES ACT OF 1933. ACCORDINGLY, NO REGISTRATION STATEMENT HAS BEEN, AND NONE WILL BE, FILED WITH THE SECURITIES AND EXCHANGE COMMISSION. TVA IS NOT SUBJECT TO THE PERIODIC REPORTING REQUIREMENTS OF THE SECURITIES EXCHANGE ACT OF 1934.

This Statement describes the business and operations of TVA as of its date and the financial condition of TVA as of the date of the financial statements included herein. Recipients of this Statement should retain it for future reference until such time as a subsequent Statement is made available by TVA, but delivery or retention of this Statement after the date hereof shall not create any implication that the information provided herein is correct at any time after the date hereof, and TVA assumes no duty to update this Statement after the date hereof, except as described above.

The date of this Information Statement is February 27, 1998.

FORWARD-LOOKING STATEMENTS

This Statement contains forward-looking statements relating to future events and future performance. Any statements regarding expectations, beliefs, plans, projections, estimates, objectives, intentions or assumptions or otherwise relating to future events or performance may be forward-looking. Some examples include statements regarding TVA's projections of future power and energy requirements, future costs related to environmental compliance, and targets for TVA's future competitive position. Although TVA believes that these statements are accurate, TVA does not guarantee their accuracy. Numerous factors could cause actual results to differ materially from those in the forward-looking statements. Such factors include, among other things, new laws and regulations, especially those related to the deregulation of electric utilities, the status of TVA as a government agency, and various environmental matters; increased competition among electric utilities; legal and administrative proceedings affecting TVA; the financial environment; performance of TVA's generating facilities; fuel prices; the demand for electricity; weather conditions; changes in accounting standards; and unforeseeable adverse events.

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Information Statement

THE TENNESSEE VALLEY AUTHORITY

TVA is one of the largest electric power systems in the United States, having produced nearly 153 billion kilowatt-hours ("kWh") of electricity in fiscal 1997. TVA is a wholly owned corporate agency and instrumentality of the United States established by the Act with the objective of developing the resources of the Tennessee Valley region.

TVA's activities fall into two types of programs — the power program and the nonpower programs. Financial accounts for the two types of activities are kept separately. Substantially all of TVA's revenues and assets are attributable to the power program, which is required to be self-supporting from the revenues it produces and capital it raises through its power program borrowings. TVA is authorized by the Act to issue Power Bonds, Discount Notes, and Other Indebtedness (collectively, "Evidences of Indebtedness") in an amount not exceeding $30 billion outstanding at any one time, the proceeds of which may be used only for the power program. See "The Basic Resolution; Power Bonds, Discount Notes and Other Indebtedness". Historically, most of the funding for TVA's nonpower programs has been provided by congressional appropriations. Additional funds have been obtained from revenues and user fees from the nonpower programs. For fiscal years 1997 and 1998 Congress appropriated $106 million and $70 million, respectively, for the nonpower programs. The appropriations act for fiscal 1998 anticipates no appropriations for TVA's nonpower programs for fiscal 1999 and thereafter and provides that essential stewardship activities are to be funded from other sources, which may include certain power revenues. For a discussion of recent legislation relating to TVA's power and nonpower programs, see "The Basic Resolution; Power Bonds, Discount Notes and Other Indebtedness" — "Recent Legislation".

In the Act, Congress has reserved the right to alter, amend or repeal the Act, but has provided that no amendment or repeal shall operate to impair the obligation of any contract made by TVA in the exercise of any power conferred by the Act. For a discussion of recent legislation relating to the TVA Act, see "The Basic Resolution; Power Bonds, Discount Notes and Other Indebtedness" — "Recent Legislation".

TVA is administered by the Board, which is composed of three persons appointed by the President and confirmed by the Senate. Appointments are for nine-year staggered terms with one term expiring with each three-year interval. The Board has sole authority for determining the rates which TVA charges for power. The Act requires the Corporation to charge rates for power which, among other things, will produce gross revenues sufficient to provide funds for operation, maintenance, and administration of its power system; payments to states and counties in lieu of taxes; debt service on outstanding Evidences of Indebtedness, including provision and maintenance of reserve funds and other funds established in connection therewith; and annual payments to the U.S. Treasury (the "Treasury") in repayment of and as a return on the government's appropriation investment in TVA power facilities. See "The Basic Resolution; Power Bonds, Discount Notes and Other Indebtedness". Such appropriation investment totaled $588 million as of September 30, 1997. See "Certain Provisions of the Tennessee Valley Authority Act" — "Payments to the Treasury".

TVA is required annually to file with the President and with the Congress a financial statement and a complete report as to the business of the Corporation. The Comptroller General of the United States is authorized to periodically audit the transactions of TVA.

Under certain conditions, TVA may borrow from the Treasury up to $150 million for a period of one year or less. Any issuance by TVA of Evidences of Indebtedness with a term of one year or longer is subject to the approval of the Secretary of the Treasury as to the issue date and maximum interest rate. The borrowing authority of TVA is treated as budget authority by the Office of Management and Budget for purposes of the budget of the United States.

Income on Evidences of Indebtedness issued by TVA is subject to various federal tax consequences. Under the Act, Evidences of Indebtedness are exempt both as to principal and interest from all taxation now or hereafter imposed by any state or local taxing authority except estate, inheritance and gift taxes. This exemption might not extend to franchise or other non-property taxes in lieu thereof imposed on corporations or to gain or loss realized upon the sale or exchange of an Evidence of Indebtedness, notwithstanding that such gain might in some cases be treated as interest income for United States federal income tax purposes.

SELECTED FINANCIAL DATA

The following selected financial data of TVA's power program for the fiscal years 1993 through 1997 have been derived from TVA's audited financial statements. These data should be read in conjunction with the audited financial statements and notes thereto (the "Financial Statements") presented herein.

Condensed Statements of Income
(dollars in millions)

	Fiscal Year Ended September 30				
	1997	1996	1995	1994	1993
Operating Revenues	$ 5,552	$ 5,693	$ 5,375	$ 5,401	$ 5,276
Operating Expenses	3,698	3,656	3,448	3,461	3,269
Operating Income	1,854	2,037	1,927	1,940	2,007
Other Income and Expense, Net	157	(10)	(91)	(59)	23
Income Before Interest Expense	2,011	2,027	1,836	1,881	2,030
Interest Expense	2,084	2,083	2,024	1,853	1,777
Allowance for Funds Used During Construction	(81)	(117)	(198)	(123)	(58)
Net Interest Expense	2,003	1,966	1,826	1,730	1,719
Net Income	$ 8	$ 61	$ 10	$ 151	$ 311
Ratio of Earnings to Fixed Charges(1)	1.00	1.03	1.01	1.08	1.18

Condensed Balance Sheet
(in millions)

	September 30				
	1997	1996	1995	1994	1993
Assets					
Current Assets	$ 1,399	$ 1,306	$ 1,088	$ 1,025	$ 1,434
Property, Plant, and Equipment	29,298	29,521	29,301	28,071	27,888
Investment Funds	561	440	260	150	—
Deferred Charges and Other Assets	2,426	2,762	2,644	2,596	1,601
TOTAL ASSETS	$33,684	$34,029	$33,293	$31,842	$30,923
Liabilities and Proprietary Capital					
Current Liabilities	$ 3,853	$ 5,101	$ 5,416	$ 4,591	$ 4,942
Other Liabilities	1,704	1,580	1,264	963	1,034
Long-Term Debt	24,152	23,320	22,583	22,206	20,954
Proprietary Capital	3,975	4,028	4,030	4,082	3,993
TOTAL LIABILITIES AND PROPRIETARY CAPITAL	$33,684	$34,029	$33,293	$31,842	$30,923

(1) Ratio of Earnings to Fixed Charges (unaudited) is calculated by dividing Net Income plus Interest Expense by Interest Expense.

COMPARATIVE FIVE-YEAR DATA

Statistical and Financial Summaries

	For the years ended September 30,				
	1997	**1996**	**1995**	**1994**	**1993**
Sales (millions of kilowatt-hours ("kWh"))					
Municipalities and cooperatives	114,771	117,035	110,245	108,073	105,566
Industries directly served	17,359	16,599	16,684	15,792	16,196
Federal agencies	7,567	6,966	7,226	4,407	2,382
Total sales	139,697	140,600	134,155	128,272	124,144
Operating revenues (millions of dollars)					
Electric					
Municipalities and cooperatives	$ 4,811	$ 4,980	$ 4,654	$ 4,582	$ 4,479
Industries directly served	464	452	460	452	472
Federal agencies	179	172	179	296	254
Other	98	89	82	71	71
Total revenues	$ 5,552	$ 5,693	$ 5,375	$ 5,401	$ 5,276
Revenue per kilowatt-hour (cents) (a)	3.90	3.99	3.94	4.03	4.06
Net winter dependable generating capacity (megawatts)					
Hydro (b)	5,384	5,298	5,225	5,242	4,885
Fossil	15,014	15,012	15,032	15,032	15,088
Nuclear units in service	5,625	5,545	3,342	3,342	3,365
Combustion turbine	2,394	2,268	2,232	2,264	2,284
Total capacity	28,417	28,123	25,831	25,880	25,622
System peak load (megawatts) — summer	26,661	25,376	25,496	23,398	23,878
System peak load (megawatts) — winter	26,670	25,995	24,676	24,723	21,666
Percent gross generation by fuel source					
Fossil	61%	65%	71%	72%	77%
Hydro	11%	11%	12%	14%	13%
Nuclear	28%	24%	17%	14%	10%
Fuel cost per kilowatt-hour (cents)					
Fossil	1.23	1.23	1.26	1.34	1.27
Nuclear (c)	.58	.56	.61	1.10	1.09
Aggregate fuel cost per kWh net thermal generation	1.04	1.06	1.14	1.31	1.25
Fuel data					
Net thermal generation (millions of kWh)	135,735	131,898	118,097	110,643	109,968
Billion Btu	1,381,837	1,338,157	1,197,295	1,120,868	1,105,395
Fuel expense (millions of dollars)	1,406	1,395	1,348	1,450	1,375
Cost per million Btu (cents)	101.73	104.22	112.61	129.40	124.42
Net heat rate, fossil only (Btu's per kWh)	10,180	10,145	10,138	10,131	10,052

(a) Excludes Department of Energy settlement payment of $160 million for the years 1993 and 1994.
(b) Includes 405 megawatts of dependable capacity from the Corps of Engineers projects on the Cumberland River system.
(c) TVA changed its method of expensing the interest component of nuclear fuel expense in 1995.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Results of Operations

Operating Environment

Net income for fiscal 1997 amounted to $8 million, down from $61 million for fiscal 1996. The reduction in earnings resulted from lower operating income attributable principally to mild weather experienced within TVA's service area during the winter and summer months of fiscal 1997, partially offset by other income related to certain investment earnings.

Net income for fiscal 1996 was $61 million compared with $10 million for fiscal 1995. This improvement was primarily driven by sales growth and increased operating efficiencies.

Operating Revenues

Operating revenues were $5,552 million in fiscal 1997 compared with $5,693 million in fiscal 1996 and $5,375 million in fiscal 1995. The $141 million decrease in fiscal 1997 as compared to fiscal 1996 was primarily due to a decrease in energy sales to municipalities and cooperatives as a result of the cool summer and warm winter during fiscal 1997. The TVA service area experienced 17 percent lower heating degree days and 11 percent lower cooling degree days during fiscal 1997 compared with fiscal 1996. Accordingly, total kWh sales decreased 0.9 billion kWh, from 140.6 billion in fiscal 1996 to 139.7 billion in fiscal 1997.

The $318 million increase in operating revenues from fiscal 1995 to fiscal 1996 was primarily due to an increase in kWh sales of approximately six billion kWh (4.5 percent), from 134 billion in fiscal 1995 to over 140 billion in fiscal 1996, combined with an increase in the revenue per kWh of approximately 0.05 cents (1.3 percent), from 3.94 cents in fiscal 1995 to 3.99 cents in fiscal 1996. The increase in kWh sales primarily resulted from overall growth within the municipalities and cooperatives segment and more extreme weather conditions in fiscal 1996.

Operating Expenses

Operating expenses increased $42 million, or 1.2 percent, from $3,656 million in fiscal 1996 to $3,698 million in fiscal 1997. The operation of the Watts Bar Unit One and Browns Ferry Unit Three nuclear units for the entire fiscal year of 1997 resulted in higher depreciation and operating expenses in fiscal 1997 as compared with fiscal 1996. These expenses, however, were partially offset by lower net fuel and purchased power expense in fiscal 1997 compared with fiscal 1996 as a result of greater generation of lower-cost nuclear power and the decrease in total power sales for fiscal 1997.

Total operating expenses increased $208 million in fiscal 1996 versus fiscal 1995, or 6.0 percent, from $3,448 million to $3,656 million. The increase resulted primarily from increased generation during fiscal 1996 and the introduction of the two nuclear units to the power system. While operating and maintenance costs increased $168 million, and depreciation and amortization expenses increased $201 million, net fuel and purchased power expense declined $165 million in fiscal 1996 compared with fiscal 1995 due to favorable fuel prices and greater off-system power sales.

Other Income and Expenses

TVA had net other income of $157 million in fiscal 1997 compared with net other expense of $10 million in fiscal 1996 and $91 million in fiscal 1995. The fiscal 1997 net other income consisted primarily of net investment earnings of the decommissioning trust funds of $138 million. The fiscal 1995 net expense was primarily composed of a $136 million charge for a voluntary early-out package offered employees, partially offset by the recognition of an $81 million deferred gain from a fiscal 1993 sale of investments.

Interest Expense

Gross interest expense remained essentially unchanged at $2,084 million in fiscal 1997 compared with $2,083 million in fiscal 1996. Total outstanding indebtedness net of unamortized discounts and other adjustments as of September 30, 1997, was $26.9 billion, with an average interest rate of 7.56 percent, compared with $27.3 billion, with an average interest rate of 7.60 percent as of September 30, 1996. The allowance for funds used during construction decreased from $117 million in fiscal 1996 to $81 million in fiscal 1997 as a result of the decline in overall construction spending.

Gross interest expense for fiscal 1996 increased $59 million from $2,024 million in fiscal 1995 to $2,083 million in fiscal 1996. This increase resulted from an increase in total outstanding debt from $26.7 billion as of September 30, 1995, to $27.3 billion as of September 30, 1996. In addition, allowance for funds used during construction declined $81 million from $198 million in fiscal 1995 to $117 million in fiscal 1996 due to the reduction of the overall level of capital spending in fiscal 1996.

Liquidity and Capital Resources

Capital Structure

Through fiscal 1959, the U.S. Government made appropriation investments of nearly $1,365 million in TVA's power program. In 1959, TVA received its current congressional approval to issue bonds to finance its growing power program. Since that time, TVA's power program has been required to be self-supporting from revenues it produces and capital it raises through its power program borrowings. Because TVA is wholly owned by the U.S. Government, TVA does not issue equity securities. As a result, TVA raises its capital requirements through the internal generation of funds or through borrowings subject to a congressionally mandated $30 billion limit. In fiscal 1997, TVA reduced its total outstanding debt by approximately $348 million. This is the first time since 1961 that TVA has ended a fiscal year with a net reduction in outstanding debt. See "Competition" for a discussion of TVA's plans to reduce its debt in the future.

Like stockholders in investor-owned companies, the U.S. Government expects to earn a return on its investment. The rate of return on this investment, plus a repayment of the initial investment, is specified by law. Total repayments and return on investment by TVA to the U.S. Treasury exceed $3 billion.

Capital Expenditures

Cash required by TVA for capital expenditures totaled $641 million, $990 million and $1.7 billion for fiscal 1997, 1996 and 1995, respectively. The reductions reflect the decline in construction spending resulting from the return of Browns Ferry Unit Three to commercial operation in January 1996, the commencement of commercial operation at Watts Bar Unit One in May 1996 and the Board's decision not to complete or restart certain other nuclear units. See "Nuclear Power Program" — "Status of Certain Nuclear Units". TVA's current forecast for capital expenditures, including capitalized interest, totals $733 million for fiscal 1998, which it expects to fund from internally generated funds.

Financing Activities

Long-term debt and cash from operations are used to finance capital expenditures. Short-term debt and cash from operations are used to manage daily cash needs. In fiscal 1997 TVA issued $3.1 billion in long-term bonds, the proceeds of which were used to refinance existing debt.

In October and December 1997, TVA issued in the public market $250 million in Power Bonds (due 1999) and $750 million in Power Bonds (due 2017), respectively, to retire existing debt.

In January 1998, TVA issued in the public market $250 million in Power Bonds (due 2018) and $1,000 million in Power Bonds (due 2038) to retire existing debt.

Subsequent to September 30, 1997, TVA monetized the call provisions on approximately $2 billion of its Power Bonds. The premiums received by TVA have been deferred and are being amortized over the term of the agreements.

Cash Flows

Net cash provided by operations for fiscal 1997, 1996 and 1995 was $1,066 million, $910 million, and $802 million, respectively. This positive trend reflects continued improvements in TVA's operations during the three-year period.

Net cash used in investing activities for fiscal 1997, 1996 and 1995 was $580 million, $1,254 million and $1,871 million, respectively. These reductions reflect the decline in construction spending from $1,868 million in fiscal 1995 to $722 million in fiscal 1997.

Net cash (used in)/provided by financing activities for fiscal 1997, 1996 and 1995 was ($425) million, $530 million and $1,119 million, respectively. The cash used in financing activities during fiscal 1997 reflects the repayment of total outstanding debt of approximately $348 million.

Accounting for the Effects of Regulation

TVA accounts for the financial effects of regulation in accordance with Statement of Financial Accounting Standards ("SFAS") No. 71, *Accounting for the Effects of Certain Types of Regulation*. As a result, TVA records certain regulatory assets and liabilities that would not be recorded under generally accepted accounting principles for non-regulated entities.

TVA has approximately $1.9 billion of regulatory assets (see Note 1 of the accompanying Financial Statements — "Other deferred charges" and "Debt issue and reacquisition costs") along with approximately $6.3 billion of deferred nuclear plants as of September 30, 1997. In the event that competition in the utility industry changes the application of SFAS No. 71, TVA would be required to evaluate such regulatory assets under the provisions of SFAS No. 121, *Accounting for the Impairment of Long-Lived Assets and Long-Lived Assets to be Disposed Of*. Statement 121 establishes requirements for evaluating and measuring asset impairments and provides that regulatory assets that are no longer probable of recovery through future revenues be charged to earnings. Such an event may have an adverse effect on future results of operations from the write-off of regulatory assets. However, TVA intends to seek full recovery of any regulatory assets that may result from TVA's transition to doing business in the competitive market.

Year 2000 Costs

TVA is evaluating the potential impact of the "Year 2000" problem on its operations. The Year 2000 problem, which is common to most companies, concerns the inability of information systems, such as computer software programs, to process date sensitive information related to the Year 2000 and beyond. TVA has established an enterprise-wide team to develop a plan and strategy, organize resources, assess the impact, and develop solutions. While it is not possible, at present, to give an accurate estimate of the cost of this work, TVA is allocating sufficient resources to address the Year 2000 problem and does not expect that such costs will be material to TVA's operations.

THE AREA SUPPLIED BY TVA

TVA supplies power in most of Tennessee, northern Alabama, northeastern Mississippi, and southwestern Kentucky, and in small portions of Georgia, North Carolina and Virginia. The population of the area served by TVA is over 7 million. Subject to certain minor exceptions, TVA may not without specific authorization by act of Congress enter into contracts which would have the effect of making it or its distributors a source of power supply outside the area for which TVA or its distributors were the primary source of power supply on July 1, 1957.

TVA is primarily a wholesaler of power. Its customers are composed of three major groups: (1) distributors, consisting of municipal and cooperative systems; (2) industries which have large or unusual loads; and (3) federal agencies. In addition, TVA has entered into exchange power arrangements with most of the surrounding electric systems.

RATES, CUSTOMERS AND MARKET

The Act delegates to the Board sole responsibility for establishing the rates which TVA charges and authorizes it to include in power contracts such terms and conditions as in its judgment may be necessary or desirable for carrying out the purposes of the Act. The Act requires the Corporation to charge rates for power which, among other things, will produce gross revenues sufficient to provide funds for operation, maintenance, and administration of its power system; payments to states and counties in lieu of taxes; debt service on outstanding Evidences of Indebtedness, including provision and maintenance of reserve funds and other funds established in connection therewith; and annual payments to the Treasury in repayment of and as a return on the Government's appropriation investment in TVA power facilities. See "The Basic Resolution; Power Bonds, Discount Notes and Other Indebtedness" — "Rate Covenant" and "Recent Legislation". Rates set by the Board are not subject to review or approval by any state or federal regulatory body. See "Competition".

A summary of power program operating revenues by customer type for each of the last five fiscal years ended September 30 is shown in the Comparative Five-Year Data, presented on page 3.

Municipal and Cooperative Distributors

TVA has long-term wholesale power contracts with 159 municipal and cooperative distributors. Such contracts are for terms of 20 years and require distributors to purchase substantially all of their electric power and energy requirements from TVA. Most distributors purchase power under a contract that requires 10 years' notice to terminate the contract and further provides that on each annual anniversary of the contract (beginning with the tenth anniversary) one additional year is automatically added to the term. Six distributors' power contract term arrangements require 15 years' notice to terminate the contract. On each annual anniversary of these contracts (beginning with the fifth anniversary) one additional year is automatically added to the term. As part of the arrangement, TVA agreed that these term arrangements are deemed to provide for adequate recovery by TVA of any investment in generation, transformation, or transmission facilities for service to the distributor. Municipal and cooperative distributors accounted for approximately 87 percent of total power revenues in fiscal 1997. See "Competition".

A number of TVA distributors, including some with the largest loads, have been expressing interest in revising the wholesale power contracts to allow them more options with respect to contract term and other matters. TVA has indicated its willingness to work with distributors to accommodate their desire for more flexibility. In this regard, the TVA Board recently approved offering distributors the option of moving from 10 or 15-year termination notice periods to a 5-year termination notice period. Such contract amendments are being conditioned upon such notice not being given during the first five years after the effective date of the revision. TVA is also agreeing that these term arrangements and existing 10 years' notice contracts are deemed to provide for adequate recovery by TVA of any investment in generation, transformation, or transmission facilities for service to the distributor. For a discussion of events which may affect TVA's relationships with its distributors, see "Competition".

TVA's wholesale power contracts contain standard provisions specifying the wholesale rates, resale rates and terms and conditions under which the power is to be distributed. Under the contracts, TVA, on a quarterly basis, may determine and make adjustments in the wholesale rate schedule with corresponding adjustments in resale rate schedules necessary to enable TVA to meet all requirements of the Act and the tests and provisions of its bond resolutions. In addition, the contracts provide for agreement between the parties on general or major changes in both the wholesale and resale rate schedules and permit TVA, if agreement is not reached, to make changes in such schedules to carry out the objectives of the Act, to meet financial requirements and tests, and to comply with the provisions of its bond resolutions.

The resale rates under which the distributors serve ultimate consumers are stipulated in the power contracts between the distributors and TVA and are revised from time to time to reflect changes in costs, including changes in the wholesale cost of power. They are designed to promote the Act's objective of providing an adequate supply of power at the lowest feasible rates.

Industries and Federal Agencies Served Directly

Contracts with industries served directly by TVA normally are for terms of 10 years but are subject to termination by TVA or the customer upon a minimum notice period that varies according to the customer's contract demand and the period of time service has been provided at that location. Industries directly served accounted for approximately 8 percent of power revenues in fiscal 1997. The power sold directly to industries is delivered under contracts at rates established by TVA. Such rates are the same as those charged by distributors to large industries (those with demand greater than 25,000 kilowatts ("kW")) they serve. Power is sold to federal agencies under the same contract terms and rates as directly served industries.

COMPETITION

The electric utility industry has become increasingly competitive in the past decade. Competition is expected to intensify in the future as a result of federally encouraged deregulation of utilities affecting the wholesale power markets and various provisions of the Energy Policy Act of 1992 ("Energy Act"). Chief among the provisions of this act which will further intensify the competitive environment are amendments (1) to the Federal Power Act that give the Federal Energy Regulatory Commission ("FERC") greater authority to order electric utilities with transmission lines to wheel (transmit) power over their systems for electric power generating entities; and (2) to the Public Utility Holding Company Act of 1935 that allow the creation of certain kinds of power generating entities without the entities or their parent corporations being made subject to regulation by the Securities and Exchange Commission under that act.

Nevertheless, a special provision in the Energy Act (the "anti-cherry picking provision") prevents the wheeling authority of FERC from being used to provide TVA-served municipal and cooperative distributors with an alternative source of power supply. That provision excludes from the wheeling authority the wheeling of electric energy that will be consumed within the area that may be served by TVA and the distributors (except for Bristol, Virginia).

Several important regulatory rulings were issued during 1996 that will continue to have a significant impact on TVA. In April 1996, FERC issued Order Nos. 888 and 889. Order No. 888 requires FERC-regulated utilities that own, control, or operate transmission lines to file nondiscriminatory open-access tariffs that offer others certain basic types of transmission service. Order No. 889 requires FERC-regulated utilities to participate in an electronic information system known as the Open Access Same-time Information System ("OASIS"), which allows for the electronic communication of information about transmission systems and services to all potential customers at the same time. This rule also requires FERC-regulated utilities to functionally separate their wholesale power marketing and transmission operations. FERC also issued a Notice of Proposed Rulemaking ("NOPR") to obtain comments on a system for reserving capacity on utilities' own and others' transmission lines.

In response to these rulings, TVA has taken steps to voluntarily comply with FERC orders. Specifically, TVA has adopted changes (effective January 1, 1997) to its existing guidelines, originally adopted by the TVA Board in 1994, which offer transmission service patterned after the open-access tariff but consistent with the TVA Act and the Energy Act. TVA posts available transmission capacity and conducts transmission business through an OASIS on the Internet. TVA has implemented a Code of Conduct based on FERC's standards contained in Order No. 889. Actions under this Code of Conduct include separating TVA's operations for transmission requests, scheduling, and transmission system security from TVA's wholesale off-system sales activities.

Although other power suppliers, under certain circumstances, may sell power in the area where TVA power is distributed, there are statutory provisions restricting TVA from expanding the area in which it is a source of power supply. It is important that TVA market power at rates competitive with other suppliers in the region. TVA believes that its ten years of stable rates during the period fiscal 1988 through fiscal 1997 have assisted distributors of TVA power in competing for new commercial and industrial loads.

In 1997 at least seven bills had been introduced in the current Congress that would mandate or promote competition in electric service at the retail level. These bills, like ones introduced during the last Congress, would also result in other major changes in the electric power industry that would significantly impact both privately owned companies and publicly owned electric power suppliers like TVA and the distributors of TVA power. The amount of government regulation, particularly for the latter, would greatly increase. In spite of their purpose to increase competition, some of these bills, as presently drafted, would not permit TVA and the distributors of TVA power to compete for customers outside the area for which TVA may be a source of power supply but would allow others to compete for customers of TVA and the distributors of TVA power. The Senate has not held formal hearings on these bills, but two days of hearings were held in the House in October 1997. Hearings on various topics of competition and electric industry restructuring have also been held in the House and Senate. TVA anticipates that in the event any retail choice legislation is enacted, such legislation would enable TVA and the distributors of TVA power to take part, reciprocally, in retail competition outside the area for which they can now be a source of electric power supply. The introduction of additional bills is expected during 1998, and this legislation is expected to receive serious congressional consideration. Although some key members of Congress have expressed an intention to complete action on retail competition legislation in 1998, final enactment remains uncertain.

Retail competition legislation raises serious issues for TVA, as it does for the rest of the electric utility industry. Among the issues which could have the greatest impact on the TVA system are: (1) the right to continue recovery of the costs of assets which would no longer be economical under full and open market competition; (2) whether TVA and its distributors will be able to sell power outside the TVA service area; (3) whether Congress will attempt to shorten the terms of TVA's present wholesale power contracts with its distributors; and (4) whether TVA rates will be regulated by FERC.

Three bills have been introduced in this Congress that would require the disposition of certain federally-owned hydroelectric system assets. None of these bills is applicable to TVA. Other such bills, which may include TVA, may be introduced. A similar proposal was not enacted during the past Congress. In TVA's opinion, enactment of such legislation is unlikely.

In today's competitive environment, some of the municipal and cooperative distributors may consider alternative wholesale supply arrangements upon expiration or termination of their power contracts with TVA. In February 1997 the city council of Bristol, Virginia ("Bristol") approved a recommendation from the Bristol Virginia Utilities Board that Bristol accept an offer from Cinergy to supply its power in the future. In April 1997 Cinergy requested that TVA provide transmission service to enable Cinergy to provide electricity to Bristol. TVA agreed to provide that service consistent with FERC's open-access transmission orders and contingent upon stranded investment cost recovery determined in accordance with applicable law. In June 1997 Cinergy initiated a FERC proceeding to require TVA to provide transmission service upon terms more favorable to Cinergy. Among the terms being challenged is TVA's demand for payment of stranded investment costs. On November 25, 1997, FERC issued an order referring the matter to an administrative law judge for an evidentiary hearing on TVA's stranded cost claim. TVA and Cinergy attempted to negotiate the terms and conditions under which TVA would provide transmission service for the supply of power to Bristol. In addition to the stranded cost issue, the parties could not agree on three operational issues. All of these issues have been submitted to FERC for resolution. On December 31, 1997, the power contract between TVA and Bristol ended, and Bristol ceased being a TVA distributor. TVA is providing transmission service to Cinergy under an interim arrangement pending resolution of the outstanding issues.

TVA's management continues to develop plans and strategies it believes will help position TVA to successfully compete in a deregulated electricity market both within the Tennessee Valley and nationwide. In July 1997 Chief Financial Officer David Smith released the TVA Ten Year Business Outlook which sets targets for a 50 percent reduction in debt and a 15 percent reduction in the total cost of power by 2007. This plan recommended a price increase for fiscal year 1998 that would result in a 5.5 percent increase in TVA's power revenues, the first such increase in ten years. In August 1997, the TVA Board approved an increase in rates designed to provide such additional power revenues, and on October 1, 1997, TVA implemented the rate increase. The Ten Year Business Outlook also calls for TVA initiatives to reduce fuel, labor, and supply costs, with a proposed reduction of approximately 700 employees in TVA's power program workforce. In addition, the plan recommended offering the opportunity to TVA's distributor customers to change their power contracts after five years from a rolling ten-year term to a rolling five-year term. The Board subsequently approved making such arrangements available to the municipal and cooperative customers served by TVA. See "Rates, Customers and Markets" — "Municipal and Cooperative Distributors". The plan has been built on assumptions that TVA believes to be reasonable, based upon today's knowledge and predictions for the future. However, future events may upset these assumptions and lead to plan modifications.

In January 1998, TVA and the Tennessee Valley Public Power Association (the "TVPPA"), which represents the interests of distributors of TVA power, issued a joint statement indicating their consensus regarding legislative positions on the restructuring of the electric utility industry. The statement recommends, among other things, that in the event customer choice legislation is enacted at the federal level: (1) the anti-cherry picking provision of the Energy Act and the territorial limitations which restrict the area in which TVA and its distributors may be a source of power (the "fence") be removed, provided that (a) the distributors' contracts are modified to shorten terms and termination notice and to allow distributors to purchase partial requirements from TVA, (b) the issue of stranded investment is addressed, and (c) TVA is required to grant access to its transmission system at reasonable charges to permit power to be transmitted to or on behalf of the distributors; (2) any recovery of TVA's stranded investment costs be subject to FERC approval, not be allowed prior to termination of a contract, and not be allowed after October 1, 2007 unless TVA and the distributor otherwise agree; (3) TVA's rights to serve new retail customers be subject to certain conditions and restrictions benefiting the distributors; (4) TVA generally be required to offer long-term, all-requirements power to distributors at wholesale rates no less favorable than that offered to new wholesale customers; (5) TVA continue to have the statutory authority to set certain terms and conditions in its all-requirements wholesale power contracts with distributors so as to facilitate the TVA Act's mandate that TVA power be distributed at the lowest feasible rates; and (6) TVA have no authority to approve retail rates or other conditions of retail service except under certain limited circumstances.

Representatives of three of the largest distributors of TVA power, the municipal power systems of Knoxville, Memphis, and Nashville, Tennessee, have also expressed positions on issues concerning restructuring of the electric utility industry, some of which differ from the positions set forth in the joint statement issued by TVA and TVPPA.

TVA anticipates that discussions with distributors regarding a wide range of issues involving the restructuring of the electric utility industry, including the issues noted above, will continue throughout the national restructuring process.

TVA has begun under the auspices of the Department of Energy ("DOE") a regional process to gather views from a wide variety of stakeholder groups as to the role the TVA power system should play in the electric utility industry after nationwide competition has begun.

In August 1995, the General Accounting Office ("GAO") issued a report which, among other things, focused on TVA's level of debt, rates, competitive position and deferred nuclear assets. The report raised the issue of whether TVA would be able to recover all the costs of its deferred nuclear assets and the financial and competitive impact this would have. While GAO is authorized to assist the Congress by evaluating government programs and activities and may make recommendations in this regard, it has no authority to order or direct that any action be taken. The report relating to TVA did not make any specific recommendations. TVA furnished to GAO a detailed response as to why the report is flawed in its analysis. GAO included TVA's response in the report appendix.

A September 1997 report by GAO on the recurring and potential future costs to the federal government of its electricity-related programs concluded with respect to TVA that (1) the federal government's initial appropriation investment in TVA and debt obligations held by the Federal Financing Bank result in no net cost to the federal government; (2) as long as TVA's power program remains in a protected position similar to a traditional regulated utility, the risk of loss to the federal government is remote; and (3) if TVA is required to compete with other electric utilities at a time when wholesale prices are expected to fall, it is reasonably possible that losses to the federal government would occur if the government decided to voluntarily take any actions to prevent default on TVA's debt service requirements, even though TVA's debt is not guaranteed by the federal government. TVA does not agree with GAO's assessment of the risk of loss to the federal government. TVA's comments on the assessment are included in Volume 2 of the GAO report.

In November 1997 the Congressional Budget Office (the "CBO") released a study discussing the federal government's role in supplying electricity and possible options for changing that role. Among other things, the study found that the government could save money over the long term by selling many of the facilities it now uses to supply electric power but that the government may want to stay in the electric power business for other reasons. With regard to TVA, the CBO estimated that, depending on the market value at which TVA could be sold, the government could currently lose up to $5.6 billion or gain up to $2.5 billion by divesting itself of TVA. The study also cites what it terms "financial challenges" that TVA now faces and will face in the near future that could affect its earnings potential and ability to cover its capital obligations. TVA expresses no opinion on the accuracy of the CBO's study or on the likelihood of any change in the government owned status of TVA.

In June 1997 Representative Bob Clement introduced a bill in the House of Representatives to create the "TVA 2000 Regional Commission". Under the bill, a twelve-member Commission (appointed by the President and by House and Senate leaders) representing a diversity of Tennessee Valley interests would complete a study and submit its report by the end of 1998. The Commission would conduct a comprehensive legal and factual study of the navigational, flood control, economic development, recreational, and economic impacts of the future structure, competitiveness and economic viability of TVA.

POWER AND ENERGY REQUIREMENTS

TVA prepares annual forecasts of future power and energy requirements as part of its planning and budgeting process. TVA's forecast procedure involves producing a range of load forecasts for the explicit purpose of bounding the range of uncertainty associated with load growth. The load forecasts are produced probabilistically. TVA believes that the high load forecast has a 90 percent probability that actual load will be less than forecast, that the medium load forecast has a 50 percent probability that actual load will be less than forecast, and that the low load forecast has a 10 percent probability that actual load will be less than forecast. TVA's current load forecast through fiscal year 2000 reflects an average annual load growth rate of 5.0 percent, 2.5 percent, and 0.5 percent for the high, medium, and low load forecasts, respectively. TVA's total system energy requirements through fiscal year 2000 reflect an average annual growth rate of 5.1 percent, 2.4 percent, and (0.3) percent for the high, medium, and low load forecasts, respectively. Numerous factors could cause actual results to differ materially from TVA's forecasts.

Various provisions in the Energy Act make changes in a wide range of laws affecting energy use and development in the United States. In addition to various other features, some of which are discussed herein, this act establishes a statutory framework for how TVA plans and selects methods for meeting future energy needs.

TVA may enter into electricity futures contracts for the sole purpose of limiting or otherwise hedging TVA's economic risks directly associated with electric power generation, purchases, and sales. The Chicago Board of Trade has proposed designating the TVA power transmission system as a hub for electricity futures contracts. This proposal is subject to review by the Commodity Futures Trading Commission.

POWER SYSTEM

TVA's power generating facilities at September 30, 1997, included 29 hydroelectric plants, 11 coal-fired plants, 3 nuclear plants, 1 pumped storage hydroelectric plant and 4 combustion turbine plants. Power is delivered to TVA customers over a transmission system of approximately 16,600 miles of lines, including 2,400 miles of extra-high-voltage (500,000 volt) transmission lines. The system interconnects with neighboring power systems at numerous points, and TVA has various types of interchange arrangements with these systems. The extent and types of interchange transactions depend upon the characteristics of the systems' loads, the management policies of the systems and other factors. Interchange arrangements are an essential part of TVA's efforts to minimize investment in electrical facilities, increase the reliability of service, effect operating economies and minimize the cost of electric energy.

In March 1997 a suit was filed in the United States District Court in Birmingham, Alabama, by four individuals challenging TVA's sale of power to Trico Steel Company, L.L.C. ("Trico"). Plaintiffs, who claimed to be employees of Trico's competitors, claimed that the TVA Act does not permit TVA to sell power to a limited liability company such as Trico; that the pricing provisions of TVA's power supply contract with Trico violated various sections of the TVA Act; and that the TVA Board's actions with respect to the Trico contract were unconstitutional because a provision of the TVA Act violates the separation of powers doctrine. Plaintiffs did not ask for monetary damages but sought to enjoin TVA from selling power to Trico and from issuing any additional power bonds until the alleged problems were corrected. TVA filed a motion asking the court to dismiss the complaint on several legal grounds. The court, on September 24, 1997, granted TVA's motion and dismissed the lawsuit. The court held that the fixing of TVA's rates is not subject to judicial review and that plaintiffs did not have standing to maintain the lawsuit since they had not suffered the requisite injury. The court did not reach the other issues in the case. The plaintiffs have appealed the decision.

During the fiscal year ended September 30, 1997, 61 percent of the power generated by the TVA coordinated system was by fossil fired plants, 28 percent by nuclear, and 11 percent by hydro. Coal consumption during this time was 39.8 million tons. Coal is purchased under contracts ranging from a single delivery to deliveries over several years. TVA coal inventory levels vary from plant to plant based upon a simulated inventory model. As of September 30, 1997, TVA had approximately 21 days' coal supply in inventory at full burn. See "Nuclear Power Program" — "Nuclear Fuel" for a discussion of TVA's nuclear fuel supplies. Management believes the sources and availability of fuel materials essential to its business should be adequate for the foreseeable future.

TVA's power system is one of the largest in the United States in capacity and in energy production. Its size permitted the construction of large facilities which resulted in lower unit costs. Most of TVA's dams were completed years ago when construction costs were far below present-day levels. Because most of the dams are multipurpose, their cost is shared by navigation, flood control, recreation and local economic development, as well as by power; thus, each purpose is served at a substantially lower cost than if the dams had been built for a single purpose.

Generating Resources

The following table summarizes the winter net dependable capacity ("NDC") in megawatts ("MW") on this coordinated system as of September 30, 1997:

	Generating Units	Winter NDC MW(1)
TVA Hydro Plants	109	3,129
TAPOCO Hydro Plants		318(2)
Corps of Engineers Hydro Plants		405(3)
TVA Pumped Storage Facility	4	1,532
Total Hydro		5,384
Fossil	59	15,014
Nuclear	5	5,625
Combustion Turbine	48	2,394
Total NDC		28,417

(1) NDC as stated is the net power output which can be obtained for a period adequate to satisfy the daily load patterns under expected conditions of operation with equipment in an average state of maintenance. For planning purposes, TVA currently estimates summer dependable total hydro capacity of approximately 5,615 MW; coal-fired capacity of approximately 14,679 MW; nuclear power capacity of approximately 5,479 MW; and combustion turbine capacity of approximately 2,045 MW, for a total summer NDC of approximately 27,818 MW.

(2) Four hydro plants owned by TAPOCO, Inc., a subsidiary of the Aluminum Company of America ("Alcoa"), are operated as part of the TVA power system. Under contractual arrangements with TAPOCO, electric power generated at these facilities is supplied to TVA. In return, TVA supplies electric power for Alcoa's aluminum plant operations located in Tennessee.

(3) The Corps of Engineers' plants on the Cumberland River system have a total installed capacity of 853 MW, of which 405 MW of NDC is available to TVA under a marketing agreement with the Southeastern Power Administration.

Under arrangements among TVA, the Corps of Engineers (the "CORPS") and the Southeastern Power Administration ("SEPA"), 8 hydro plants of the CORPS comprising the Cumberland River system are operated in coordination with the TVA system. These arrangements further provide for capacity (405 MW) and energy from the Cumberland River system to be supplied to TVA by SEPA at the points of generation, and the price paid for the power to be based on the operating and maintenance expenses and amortization of the power facilities. A portion of the output of the Cumberland River system is also made available to SEPA's customers outside the TVA region. The agreement with SEPA covering these arrangements for power from the Cumberland River system can be terminated upon three years' notice.

TVA has contracted with Choctaw Generation, Inc. to purchase and take delivery of up to 440 MW of power over a 30-year term from a lignite power plant to be constructed in Mississippi, contingent upon satisfactory completion of all necessary environmental reviews. Commercial operation of the plant is currently scheduled for January 2001. The owner of the facility has construction and operating risks, and if the owner fails to deliver the required energy, the owner will be responsible for securing replacement power for TVA at the contractually agreed price.

Integrated Resource Plan

In December 1995, the Board approved TVA's Integrated Resource Plan ("IRP") which presents TVA's strategy for meeting future customer energy demands. The IRP identifies a 25-year least-cost energy resource strategy for TVA's power system. TVA's IRP strategy relies on a portfolio of energy resource options that made up the best strategies evaluated for the TVA power system. These strategies performed well across all of the IRP evaluation criteria including debt, rates, costs, reliability, and environmental impacts and regulations. These strategies are designed to enable TVA to respond to future demands in a manner that maintains flexibility and enhances its competitive position. Included in the portfolio are customer service options such as energy conservation and load management; supply side options, including power purchased from other producers; and investigation and use of renewable energy.

Since the final IRP was issued in December 1995, TVA has undertaken the following actions identified in the IRP.

1. Purchased 2,000 MW of options of future peak and base-load capacity to meet future power needs in the Tennessee Valley region.

2. Issued an Environmental Impact Statement evaluating the conversion of Bellefonte Nuclear Plant to a fossil fuel-fired plant. A feasibility study performed by an outside team of technical and financial experts concluded that one of the most economical fossil conversion strategies was to complete Bellefonte as a natural gas-fired combined-cycle plant. In addition, TVA submitted a proposal to DOE to complete Bellefonte as a nuclear plant and to operate it to produce tritium for DOE in addition to electricity. TVA also proposed providing irradiation services to produce tritium at Unit One of the Watts Bar Nuclear Plant. Further action will depend on DOE's evaluation of and response to the TVA proposals and other potential options to produce tritium. See "Nuclear Power Program" — "Status of Certain Nuclear Units".

3. Implemented or began pilot programs for the following energy service programs:

- Residential demand-side management programs such as a heat pump retrofit program, a new homes program, an energy self-audit and student-audit program, and a low income demonstration program.
- An energy service company pilot designed to encourage the efficient use of electricity in the commercial and industrial sectors.
- Beneficial electrification programs designed to encourage efficient heating and air conditioning in residential and commercial establishments, commercial cooking, residential security lighting, and industrial electrotechnologies.

- Load management activities which include water heater control, storage water heaters, and real time pricing.

4. Continued research into several renewable energy technologies such as wind, biomass, and landfill methane.

TVA continues to review and update its resource plans. To date, several internal options have been approved including upgrades to combustion turbine units, upgrades to Raccoon Mountain Pumped Storage Plant, and fossil plant improvements. Discussions with suppliers of peaking power are underway to determine if other options should be pursued.

NUCLEAR POWER PROGRAM

Overview

TVA has five operating nuclear units at three locations: Sequoyah Units One and Two, Browns Ferry Units Two and Three and Watts Bar Unit One. Construction activities at three additional units have been suspended and one licensed unit remains in an inoperative status. See detailed discussions on all operating and inoperative nuclear units in the sections below and Note 2 of the accompanying Financial Statements.

Sequoyah

Sequoyah is a two-unit plant located approximately 7.5 miles northeast of the city limits of Chattanooga, Tennessee, with pressurized water reactors supplied by Westinghouse Electric Corporation. Each unit is rated at 1,147 MW net electrical output. TVA received an Operating License for Unit One in 1980, and the unit began commercial operation in 1981. TVA received an Operating License for Unit Two in 1981, and the unit began commercial operation in 1982. The Operating Licenses expire 40 years after issuance. The plant was designed and built and is operated by TVA. TVA voluntarily shut down both units in 1985 in response to technical and operational concerns.

Both Sequoyah units returned to commercial operation in 1988 and were removed from the NRC's list of plants that require close monitoring in 1989. Sequoyah Units One and Two have recorded an 82.5 average percent equivalent availability for the three years ending September 1997. (The "equivalent availability" is the ratio of the energy a unit could have generated, if called on, to the energy the unit would have produced if it had run at full load over the entire period, expressed as a percentage).

Browns Ferry

Browns Ferry is a three-unit plant located approximately 10 miles southwest of Athens, Alabama, with boiling water reactors supplied by General Electric Company. Each unit is rated at 1,065 MW net electrical output. The plant was designed and built and is operated by TVA. TVA received Operating Licenses for Units One, Two, and Three in 1973, 1974 and 1976, respectively. They began commercial operation in 1974, 1975 and 1977, respectively. The Operating Licenses for these units expire 40 years after issuance. Units One, Two and Three were voluntarily shut down by TVA in 1985 in response to technical and operational concerns.

Browns Ferry Unit Two was returned to commercial operation in 1991 and was removed from the NRC's list of plants requiring continued close monitoring in 1992. Browns Ferry Unit Two has recorded an 86.8 average percent equivalent availability factor for the three years ending September 1997.

Browns Ferry Unit Three was restarted in November 1995 and returned to commercial operation in January 1996. In June 1996 the NRC removed Browns Ferry Unit Three from the list of plants warranting close monitoring. Browns Ferry Unit Three recorded a 90.9 percent equivalent availability factor from restart through September 30, 1997.

Browns Ferry Unit One has been idled since March 1985. Major modifications would be required to bring the plant to current standards. At September 30, 1997 the undepreciated cost of Browns Ferry Unit One was \$80 million. In 1994 preliminary cost estimates based on IRP information indicated that cost associated with returning Unit One to service would have been between $1.2 and $3.2 billion. See "Status of Certain Nuclear Units" for discussion of the status of Browns Ferry Unit One.

Watts Bar

Watts Bar is a two-unit power plant located approximately 50 miles northeast of Chattanooga, Tennessee, with pressurized water reactors supplied by Westinghouse Electric Corporation. Unit One is rated at 1,154 MW net electrical output. The plant was designed and has been built to its present level of completion by TVA. The Construction Permit for Unit Two expires in December 1999.

Although physical construction of Watts Bar Unit One was substantially complete in 1985, efforts to obtain an Operating License were delayed due to numerous safety concerns. Overall plant design was reverified and extensive modifications were made. The NRC granted TVA a license to operate Unit One at up to five percent of rated power in November 1995 and at full power in February 1996. Watts Bar Unit One successfully completed all power ascension testing activities and commenced full power commercial operation in May 1996. The Operating License for Unit One expires 40 years after issuance. Since beginning commercial operation, the plant has operated at an 82.1 percent equivalent availability factor through September 30, 1997.

In 1988, TVA suspended construction activities at Watts Bar Unit Two because of a reduction in the forecasted load growth. Total investment in Unit Two at September 30, 1997, was $1.7 billion, including capitalized interest. In 1994 preliminary cost estimates based on IRP information indicated that the cost associated with completing Unit Two would have been between $1.1 and $2.9 billion. See "Status of Certain Nuclear Units" for discussion of the status of Unit Two.

Bellefonte

Bellefonte is a two-unit power plant located approximately 59 miles southwest of Chattanooga with pressurized water reactors supplied by Babcock & Wilcox Company rated at 1,212 MW net electrical output each. The plant was designed and has been built to its present level of completion by TVA. Construction Permits were obtained from the NRC for both units in December 1974.

TVA deferred construction activities on Bellefonte Unit Two because of a reduction in forecasted load growth in October 1985. Construction activity was deferred on Unit One in July 1988. In March 1993, TVA notified the NRC of its plans to resume completion activities at Bellefonte, but no construction activities have occurred since 1988. Construction Permits for Unit One and Unit Two have been extended by the NRC to 2001 and 2004, respectively.

As of September 30, 1997, TVA had $4.6 billion, including capitalized interest, invested in these units. See "Status of Certain Nuclear Units" for discussion of Bellefonte's current status. In 1994 preliminary cost estimates based on IRP information indicated that cost associated with completing the Bellefonte units would have been between $1.3 and $3.5 billion for Unit One and $900 million and $2.4 billion for Unit Two.

Status of Certain Nuclear Units

Preliminary cost estimates, utilizing the IRP (see "Power System" — "Integrated Resource Plan"), showed that completing the units at Bellefonte and Watts Bar Unit Two may not be economically feasible. As a result, the Board in December 1994 announced a major change in policy declaring that TVA will not, by itself, complete Bellefonte Units One and Two and Watts Bar Unit Two as nuclear units. In addition, the Board decided that Browns Ferry Unit One should continue in its inoperative status.

TVA's IRP identified as a viable option the conversion of the Bellefonte facility to a combined-cycle plant utilizing natural gas or gasified coal. In 1997 an independent team of technical and financial experts completed a feasibility study to evaluate options for the conversion of Bellefonte Nuclear Plant to a fossil fuel-fired plant. The feasibility study indicates that one of the most economical fossil conversion strategies is to complete Bellefonte as a natural gas-fired combined-cycle plant. TVA also issued an Environmental Impact Statement ("EIS") assessing the environmental impacts of various fossil conversion options. The EIS identified the natural gas-fired combined-cycle plant alternative as the preferred option. In addition, TVA submitted a proposal to DOE to complete Bellefonte as a nuclear plant and to operate it to produce tritium for DOE in addition to electricity. TVA also proposed providing irradiation services to produce tritium at Unit One of the Watts Bar Nuclear Plant. Further action will depend on DOE's evaluation of and response to the TVA proposal and DOE's other potential options to produce tritium.

At September 30, 1997, TVA's total investment in Bellefonte Units One and Two, Watts Bar Unit Two and Browns Ferry Unit One was $7.0 billion. The future decisions on these units will ultimately impact the method of cost recovery, and the TVA Board has determined that it will establish rate adjustments and operating policies to ensure full recovery of the cost of these units and compliance with the requirements of the TVA Act.

Because of extensive regulatory requirements and the resulting delays which are often very lengthy, estimates of the cost to complete nuclear plants have typically been unreliable. No assurance can be given that TVA's cost estimates would not be changed significantly if a decision is made to complete or operate any of the inoperative units.

Nuclear Fuel

TVA owns all nuclear fuel held for its nuclear units (operating and deferred). The net book value of such fuel was $840 million as of September 30, 1997. See Note 2 of the accompanying Financial Statements. TVA currently has sufficient inventory to last until late 1998.

TVA's investment in the fuel being used in the Sequoyah, Watts Bar and Browns Ferry units is being amortized and accounted for as a fuel expense. The Bellefonte initial cores have been defabricated and uranium from these cores has been used in the Sequoyah and Browns Ferry units with the net book value assigned accordingly.

Nuclear Waste

Spent Nuclear Fuel

The Nuclear Waste Policy Act of 1982 (the "NWPA") provides that the federal government has the responsibility for the permanent disposal of spent nuclear fuel but charges each nuclear power system with the responsibility for the cost of such permanent disposal. The NWPA requires each nuclear power system to enter into a disposal contract with DOE for such material. The contract requires each nuclear power system to pay a fee which is currently one mill per kWh for the net electricity generated by each of its reactors and sold. Although it is uncertain when DOE will be able to begin accepting spent nuclear fuel, TVA believes its spent fuel efforts will ensure that sufficient cost-effective at-reactor storage is available to meet all of TVA's spent fuel storage requirements until DOE is prepared to accept TVA's spent fuel.

TVA presently has the capability to store its spent fuel at Sequoyah through the year 2002, at Browns Ferry Units One and Two through the year 2011, and at Browns Ferry Unit Three through the year 2000. Based on a one unit operation, Watts Bar storage capability will be sufficient until 2018. Plans are in place to extend storage capacity at Browns Ferry Unit Three until 2006. TVA plans to extend storage capability through life-of-plant if necessary by using higher density racks in its existing storage pools or dry storage casks. Additional storage capacity increases will require NRC approval. However, all of the above methods of extending storage capability have been licensed by the NRC at other facilities.

Low-Level Radioactive Waste

Disposal costs for low-level radioactive waste that result from normal operation of nuclear units have increased significantly in recent years. Pursuant to the Low-Level Radioactive Waste Policy Act, each state is responsible for disposal of low-level waste generated in that state. States may form regional compacts to jointly fulfill their responsibilities. The States of Tennessee and Alabama (where TVA nuclear plants are located) have joined with other southeastern states to form the Southeast Compact Commission for Low-Level

Radioactive Waste Management. This commission regulates the siting of new disposal facilities and the disposal of low-level waste within the southeastern states.

Until July 1995, the low-level waste generators located in the Southeastern states were required to dispose of their waste at the Barnwell, South Carolina disposal facility. South Carolina has withdrawn from the Southeast Compact Commission in order to open the Barnwell facility to all states except North Carolina. The states participating in the Southeast Compact Commission have selected North Carolina as the host state to select, license, and construct a new disposal site. TVA plans to continue to use the Barnwell facility for low-level radioactive waste disposal until the North Carolina facility is opened. Should either or both of the disposal facilities close unexpectedly, low-level radioactive waste will be stored in on-site facilities at the TVA nuclear plants. These facilities are sized to handle any anticipated storage needs for the foreseeable life of the plants.

Nuclear Insurance

The indemnification and limitation of liability plan afforded the United States nuclear industry by the Price-Anderson Act was extended for an additional 15 years in 1988, with certain provisions of the Price-Anderson Act now due to expire on August 1, 2002. The 1988 amendments and the 1993 inflation adjustment to the Price-Anderson Act substantially increased the limit of liability from an accident at an NRC-licensed reactor, and this amount is now approximately $8.7 billion ($79 million for each of the NRC-licensed reactors in the United States), composed of primary and secondary layers of financial protection. For further information about this nuclear liability insurance and its deferred premium see Note 10 of the accompanying Financial Statements. TVA, in accordance with industry practice, maintains certain liability insurance coverage for workers at the nuclear sites.

NRC regulations require nuclear power plant licensees to obtain, and TVA has acquired, onsite property damage insurance coverage of $1.06 billion per nuclear site. Some of the nuclear property insurance may require the payment of retrospective premiums of up to approximately $32.0 million (retrospective premium amount as of November 1997) in the event that losses by another insured party or TVA exceed available funds. In accordance with NRC regulations, the proceeds of nuclear property insurance are used first to ensure that the reactor is in safe and stable condition and that it can be maintained in a condition that prevents significant risk to the public. Next, the proceeds go for decontamination or, if necessary, decommissioning the reactor. Any excess proceeds insure against casualties to property.

Decommissioning

In prior years, the excess of the annual decommissioning provision over earnings from any investments designated for funding decommissioning costs has been charged to depreciation expense. Investments were made in amounts sufficient to fully fund all estimated decommissioning costs. Effective for fiscal 1998, TVA changed its method of accounting for decommissioning costs and related liabilities. TVA's current accounting policy recognizes, as incurred, all obligations related to closure or removal of its nuclear units. The liability for closure is measured at the present value of the estimated cash flows required to satisfy the related obligation and discounted at a determined risk free rate of interest. The corresponding charge to recognize the additional obligation was effected through the creation of a regulatory asset. TVA further modified its method of accounting for decommissioning costs such that earnings from decommissioning fund investments, amortization expense of the decommissioning regulatory asset, and interest expense on the decommissioning liability are deferred in accordance with Statement of Financial Accounting Standards No. 71, "Accounting for the Effects of Certain Types of Regulation." The book value of TVA's decommissioning fund investments was $553 million at September 30, 1997. See Notes 1 and 10 of the accompanying Financial Statements.

ENVIRONMENTAL MATTERS

TVA's activities are subject to various federal, state, and local environmental statutes and regulations. Major areas of regulation affecting TVA's activities include air pollution control, water pollution control, and management and disposal of solid and hazardous wastes. Because TVA is a federal agency, it is subject only to those state and local environmental requirements for which Congress has clearly waived federal agency immunity. Respecting the major environmental areas (air, water and waste), limited waivers have been enacted by Congress. TVA's activities may also be subject to other narrower environmental requirements or to environmental requirements which affect only federal activities.

TVA has incurred and continues to incur substantial capital expenditures and operating expenses to comply with environmental requirements. See Note 10 of the accompanying Financial Statements. Because of the continually changing nature of these requirements, the total amount of these costs is not now determinable. It is anticipated that environmental requirements will become more stringent and that compliance costs will increase, perhaps by substantial amounts.

Air Pollution

Under the Clean Air Act, the United States Environmental Protection Agency (the "EPA") has promulgated national ambient air quality standards for certain air pollutants, including sulfur dioxide, particulate matter and nitrogen oxide. Coal-fired generating units are major sources of these pollutants. TVA also operates other smaller sources. The States of Alabama and Tennessee and the Commonwealth of Kentucky have promulgated implementation plans which regulate sources within their boundaries, including TVA sources, in order to achieve and maintain the national ambient standards. TVA has installed control equipment and employs control strategies to comply with applicable state-established emission limitations. TVA estimates that it spent about $1.4 billion in capital costs on air pollution control activities prior to the 1990 Clean Air Act Amendments.

The acid rain control provisions of the 1990 Amendments to the Clean Air Act establish a number of new requirements for utilities. These requirements are being implemented by EPA and states in two phases. TVA's Phase I affected units were brought into compliance at a capital cost of approximately $750 million (exclusive of interest expenses). TVA's current Phase 2 compliance strategy is expected to result in capital costs of approximately $550 million.

Several EPA developments may affect the air pollution control requirements that are applicable to TVA's fossil plants. States and EPA are considering how the long-range transportation of both nitrogen oxide, which contributes to the formation of ozone, and ozone may contribute to violations of the ozone ambient air quality standard in downwind states. Eight northeastern states have petitioned EPA to order upwind states — including Alabama, Kentucky, and Tennessee — to reduce their nitrogen oxide emissions. Also, EPA has proposed that nitrogen oxide emissions be reduced in 22 eastern states including Alabama, Kentucky, and Tennessee. Most of these reductions would come from utility units. EPA has also made the ozone ambient standard and the particulate matter standard more stringent along with proposed rules to reduce regional haze. These actions may lead to additional reductions of utility nitrogen oxide and sulfur dioxide emissions beyond those required by the acid rain provisions of the 1990 amendments. The costs for such additional reductions are unknown at this time but could exceed $2.5 billion.

The ozone ambient standard was exceeded in the Memphis, Tennessee area in the summer of 1995, and this triggered the Memphis-Shelby County ozone maintenance-contingency plan. Under this contingency plan, sources of nitrogen oxide within Shelby County can be required to further reduce emissions. TVA has agreed to reduce Allen Fossil Plant's nitrogen oxide emissions to help address this problem. The costs of doing this will not be substantial.

Under DOE's Climate Challenge Program, TVA entered into an agreement with DOE in 1993 to reduce greenhouse gas emissions (e.g., carbon dioxide) by 22.7 million tons by the year 2000. The costs of this voluntary effort have not been substantial. Efforts are being made internationally to obtain binding commitments from countries to reduce their greenhouse gas emissions. Negotiations were completed in December 1997 on a United Nations framework convention on climate change. Under this convention, some industrialized nations, including the United States, will have to reduce their greenhouse gas emissions. If this treaty is approved by the United States, utilities would likely be required to reduce their greenhouse gas emissions, and the cost to TVA could be substantial.

Water Pollution

Under the Clean Water Act, every point source which discharges pollutants into waters of the United States must obtain a National Pollutant Discharge Elimination System ("NPDES") permit specifying the allowable quantity and characteristics of the pollutants discharged. TVA's various point sources have received NPDES permits, including all of its major generating units. Compliance with NPDES requirements has necessitated substantial expenditures and may require additional, substantial expenditures in the future as NPDES permits come up for renewal and applicable requirements are made more stringent.

The Clean Water Act allows the permitting authority to establish thermal limits less stringent than the water quality criteria if the discharger can demonstrate that the alternate limit will assure protection and propagation of a balanced, indigenous aquatic population. TVA has now been issued alternate limits at several of its facilities, and it is meeting these limits. EPA has underway a rulemaking that would address the design of water intakes. The rulemaking is not expected to be completed for several years but could require changes to be made at TVA facilities. The cost of such changes is uncertain.

Solid and Hazardous Waste Management

Under the Resource Conservation and Recovery Act ("RCRA"), the storage, transportation, and disposal of hazardous wastes are regulated by EPA and the states. RCRA also allows EPA and the states to regulate solid wastes, and the states have detailed permitting programs for this. TVA has detailed procedures in place designed to ensure compliance with all applicable requirements for the management of hazardous wastes. In addition, TVA has instituted an approved supplier list for hazardous waste disposal contractors under which such contractors' financial status, compliance history, and physical facilities and operations can be reviewed before they are allowed to treat or dispose of any of the hazardous wastes generated by TVA facilities. TVA does not itself operate any hazardous waste disposal or treatment facilities but does operate two permitted hazardous waste storage facilities in Muscle Shoals, Alabama. TVA has obtained or is in the process of obtaining solid waste disposal permits for the solid waste disposal areas (e.g. fly ash, scrubber sludge, demolition materials and asbestos) it operates at some of its plant sites. TVA's costs in this area have not been substantial, but applicable requirements are constantly changing and are expected to become more stringent.

Under the Comprehensive Environmental Response, Compensation, and Liability Act ("CERCLA"), the release and cleanup of hazardous substances are regulated. Certain persons who are associated with the release of hazardous substances to the environment can be held responsible for their cleanup, regardless of when the substances were released or when the specific person may have been associated with the substance. This liability under CERCLA is generally viewed as joint and several. TVA, in a manner similar to other industries and power systems, has generated or used hazardous substances over the years. In connection with these activities, TVA has been identified as a potentially responsible party with respect to three non-TVA sites at which TVA hazardous substances were disposed and which have not yet been resolved. In addition, TVA is currently investigating two other sites at which TVA is either an owner or a partial owner and for which TVA may have cleanup responsibilities by virtue of its control of the property. TVA's potential liabilities for its share of cleanup costs at these sites are uncertain but in total should be less than $10 million.

Miscellaneous

Polychlorinated biphenyls ("PCBs") have been widely used as insulating fluids in electric equipment (e.g., transformers and capacitors). Use of such equipment and the cleanup of released PCBs are regulated by EPA under the Toxic Substances Control Act. The TVA power system uses thousands of pieces of equipment which contain some level of PCBs. Most of this equipment can continue to be operated under EPA's PCB regulations for the remainder of its useful lives, but TVA is phasing out much of this equipment as a matter of policy. The cost of phasing out the remainder of this equipment should not exceed $40 million (equipment replacement and disposal costs) but cannot be accurately determined at this time. TVA has in place detailed procedures to conform its operations to EPA's PCB regulations, and it has not incurred substantial costs in this area.

Many of TVA's facilities were constructed at a time when asbestos was the insulation of choice by industry. Asbestos materials now require special handling and disposal when they are removed. Although not required, TVA is removing or encapsulating asbestos as appropriate.

There is public concern about whether there are adverse health effects from exposure to electric and magnetic fields ("EMF"). There are many sources of EMF, including electric transmission lines. Recent research, including a report from a National Academy of Sciences organization (the "NAS"), has confirmed that there is no conclusive evidence that EMF causes adverse health effects. A report by the National Cancer Institute on the scientific evidence has now confirmed the NAS conclusions. However, research in this area continues. Substantial costs could be incurred by electric systems, including TVA, if EMF levels from transmission lines have to be reduced, but this appears unlikely at this time.

As a federal agency, TVA is required to consider the potential environmental effects of major federal actions affecting the quality of the human environment under the National Environmental Policy Act (the "NEPA") and implementing regulations and to make these evaluations available to the public. TVA has incorporated the NEPA review process into its decision making process. NEPA-related costs are incurred continuously but not in substantial amounts.

INSURANCE

TVA does not generally carry property damage or public liability insurance except as may be required or appropriate with respect to nuclear facilities and except to the extent it may do so as part of an owner-controlled insurance program it has implemented for some large contracts requiring on-site labor. Liability for service-connected injuries to employees is governed by the Federal Employees' Compensation Act. See "Nuclear Power Program" — "Nuclear Insurance" herein and Note 10 of the accompanying Financial Statements for additional information with respect to insurance.

MANAGEMENT

TVA is administered by a board of directors composed of three persons appointed by the President and confirmed by the Senate. The Board and selected officers, their ages, their years of employment with TVA and principal occupations for recent years are as follows:

Name and Title	Age	Year Commenced Employment	Year Term Expires
Craven Crowell Chairman	54	1993	2002
Johnny H. Hayes Director	57	1993	2005
William H. Kennoy Director	61	1991	1999
Joseph W. Dickey Chief Operating Officer & Executive Vice President, Fossil and Hydro Power Group	53	1991	
Oswald J. Zeringue Chief Nuclear Officer & Executive Vice President	52	1989	
David N. Smith Chief Financial Officer & Executive Vice President, Financial Services	54	1995	
Norman A. Zigrossi Chief Administrative Officer & Executive Vice President, Business Services	62	1986	
Edward S. Christenbury General Counsel and Secretary	56	1987	

Mr. Crowell was appointed to the Board in July 1993. Prior to his current position, he served as Chief of Staff for Jim Sasser, Tennessee's then senior U.S. Senator (1989-1993), as Vice President of TVA's Office of Governmental & Public Affairs (1988-1989), and as TVA's Director of Information (1980-1988).

Mr. Hayes was initially appointed to the Board in July 1993 to fill the remainder of a Board term which expired in May 1996. Subsequently he received a recess appointment to the Board and was then appointed for a full term (until 2005). Prior to his current position, he served as the State of Tennessee's Commissioner of Economic and Community Development (1992-1993) and as Tennessee's Commissioner of Employment Security (1991-1992).

Mr. Kennoy was appointed to the Board in April 1991. Prior to his current position, he served as President of Kennoy Engineers for twenty-five years.

Mr. Dickey was named Chief Operating Officer in February 1994 and additionally was named Executive Vice President in October 1996. Prior to his current position, he served as TVA's Senior Vice President, Fossil and Hydro Power (1991-1994), as Vice President of Power Resources (Florida Power & Light Co.) (1988-1991), and as Vice President, Nuclear Energy (Florida Power & Light Co.) (1985-1988).

Mr. Zeringue was named Chief Nuclear Officer & Executive Vice President in 1997. Prior to his current position, he served as Senior Vice President, Nuclear Operations (1993-1997), as Browns Ferry Site Vice President (1989-1993), and as Plant Manager of Palo Verde Nuclear Station, Arizona Public Service Company (1987-1989).

Mr. Smith was named Chief Financial Officer in January 1995 and additionally was named Executive Vice President, Financial Services, in October 1996. Prior to his current position, he served as Executive Director of Odyssey Financial (1993-1994), as Vice President of Finance of LTV Corporation (1991-1993), and as Assistant Treasurer and Director of Corporate Finance of LTV Corporation (1986-1991).

Mr. Zigrossi was named Chief Administrative Officer in February 1994 and additionally was named Executive Vice President, Business Services, in October 1996. Prior to his current position, he served as TVA's President, Resource Group (1992-1994) and as TVA's Inspector General (1986-1992).

Mr. Christenbury assumed the position of General Counsel of TVA in January 1987. Prior to his current position, he served as an Assistant General Counsel at the NRC (1980-1987).

EMPLOYEES

On December 31, 1997, TVA had about 14,200 employees, of which approximately 5,200 were trades and labor employees. Neither the federal labor laws covering most private sector employers, nor those covering most federal agencies are applicable to TVA; however, the Board has a longstanding policy of recognizing and dealing with recognized representatives of its employees. TVA employees are prohibited by federal law from engaging in strikes against TVA. In 1992, TVA entered into separate long-term agreements with the Tennessee Valley Trades and Labor Council ("Council"), the Salary Policy Employee Panel ("Panel"), and the International Brotherhood of Teamsters ("Teamsters"). One agreement recognized the Panel for collective bargaining purposes for 20 years. The other recognizes the Council and Teamsters for collective bargaining purposes for 15 years. About 77 percent of TVA's employees are in these bargaining units. TVA's labor agreements typically provide for negotiation of most provisions except monetary matters about every three years; wage and salary and benefit negotiations or adjustments generally occur annually. Unresolved disputes over rates of pay for trades and labor employees are resolved by binding decisions of the Secretary of Labor, while pay and monetary benefits disputes for other represented employees are resolved through binding arbitration. TVA's hourly construction, modification and supplemental maintenance work is now performed by contractors primarily under project labor agreements negotiated by TVA and the Council. Permanent craft operating and regular maintenance work continues to be performed by annual TVA employees represented by the Council for operating and maintenance employees, and by the Teamsters for materials handling work.

During mid-1997, negotiations between TVA and the Council (which is comprised of six unions representing annual trades and labor employees, including those working inside the power plants) were delayed for about three months because of lawsuits filed by some Council unions, but there are now no legal restrictions on continuance of negotiations. The parties reopened negotiation sessions but have since reached an impasse. The collective bargaining agreement with the Council has no specific expiration date; however, it contains provisions for possible expiration of major parts of the agreement upon six months' notice, which notice TVA gave the Council in June 1997. With the expiration of parts of the agreement on December 31, 1997, TVA exercised its right to give a 90-day notice to reopen the remainder of the agreement with the Council, and potentially to cancel the agreement. In October, TVA concluded negotiations with the Teamsters for a new agreement.

The agreements with the Panel (which had been comprised of five unions representing white collar employees) also had no expiration date but provided for possible expiration of major parts of the agreement in 1999, upon 12 months' notice. However, in September 1997, two unions formerly belonging to the Panel, which together represent about 64 percent of the employees represented by Panel-affiliated unions, notified TVA and the Panel that they had disaffiliated from the Panel. After the Panel failed to provide TVA assurances that it could fulfill its contractual obligation to speak for all Panel unions, TVA informed the Panel that because it was in material breach of the TVA-Panel agreement, it was no longer appropriate for TVA to continue bargaining with the Panel. TVA, however, informed each of the five affected unions that it would recognize and separately bargain with each for their existing separate bargaining unit and that it was willing to extend to each of them, on an interim basis, the terms of the former TVA-Panel agreement, to the extent applicable to individual unions. To date, the two unions which notified the Panel of their disaffiliation have agreed to interim agreements, and each of these unions has concluded negotiations for a new separate agreement with TVA. Another former Panel union has accepted TVA's offer of an interim agreement through April 30, 1998, and agreed to negotiate for a new separate agreement, without prejudice to either party's position regarding the current validity of the TVA-Panel agreement. Those negotiations have concluded without agreement, but that union is polling its membership regarding TVA's last offer. A fourth Panel union has yet to accept TVA's offer of an interim agreement. (The bargaining unit for the remaining union has been merged into one of the other former Panel unions with whom TVA has reached agreement.)

Salaries of regular TVA employees are limited by a federal pay cap (Executive Level IV, currently $118,400). This had led in the past to difficulties in the recruitment and retention of top management talent, and continues to be an issue which TVA must face in its recruitment and retention efforts. The impact of the pay cap has been alleviated somewhat by the increases in TVA's pay cap since January 1990 from $80,700 to $118,400. TVA has also addressed this issue by developing and implementing supplementary compensation arrangements, which have substantially reduced the impact of the pay cap. In TVA's opinion, the implementation of these arrangements is within TVA's legal authority. The GAO has expressed the opinion that some of these arrangements are not within TVA's legal authority. However, GAO has no authority to issue binding legal opinions on this matter or to stop any TVA payments. Congress is aware of TVA's supplemental compensation arrangements and has not taken any action that would undermine TVA's position that the arrangements are within its legal authority. Recently, TVA's executive compensation arrangements have come under increasing scrutiny from some members of Congress. It is possible that this scrutiny could result in legislative proposals to limit TVA's authority in this area. TVA has recently contracted with a national compensation management firm to determine whether TVA's executive compensation arrangements are appropriate to attract and retain the caliber of executive talent required to manage TVA's power system.

In October 1995, the President issued an Executive Order requiring Government corporations, including TVA, to submit information to the Office of Management and Budget ("OMB") on bonuses paid to its senior executives. Those bonuses and the information supporting them were last reported to OMB in December 1997 and were also publicly disseminated. OMB approval of TVA's bonuses is not required.

CERTAIN PROVISIONS OF THE TENNESSEE VALLEY AUTHORITY ACT

The following summarizes certain provisions of the Act.

Payments in Lieu of Taxes

TVA is not subject to federal income taxes or to taxation by states or their subdivisions. However, the Act requires TVA to make payments in lieu of taxes to states and counties in which the power operations of the Corporation are conducted. The basic amount is 5 percent of gross revenues from the sale of power to other than federal agencies during the preceding year, with the provision for minimum payments under certain circumstances.

Payments to the Treasury

The Act requires TVA to make certain payments into the Treasury each year from Net Power Proceeds in excess of those required for debt service as a return on and reduction of the Appropriation Investment. Net Power Proceeds are defined as the remainder of TVA's Gross Power Revenues after deducting the cost of operating, maintaining and administering its power properties (including multiple-purpose properties in the proportion that multiple-purpose costs are allocated to power) and payments to states and counties in lieu of taxes, but before deducting depreciation accruals or other charges representing the amortization of capital expenditures, plus the net proceeds of the sale or other disposition of any power facility or interest therein.

Acquisition of Real Estate

The Act empowers TVA to acquire real estate in the name of the United States of America by purchase or by exercise of the right of eminent domain, "and thereupon all such real estate shall be entrusted to the Corporation as the agent of the United States to accomplish the purposes of [the] Act". Since nearly all of TVA's properties, including powerhouses and transmission line rights-of-way, constitute real estate, title to which is held in the name of the United States and entrusted to TVA as agent of the United States, all references in this Statement to "TVA properties" and the like, and to the amounts invested therein, should be read and construed in the light of this provision of the Act.

THE BASIC RESOLUTION; POWER BONDS, DISCOUNT NOTES AND OTHER INDEBTEDNESS

TVA's Power Bonds are issued pursuant to Section 15d of the Act and pursuant to the Basic Resolution. At December 31, 1997, TVA had outstanding U.S. $23.1 billion and DM 1.5 billion (issued in September 1996) principal amount of Power Bonds. Power Bonds may be issued only to provide capital for TVA's power program (including refunding any Evidences of Indebtedness issued for like purposes) and only as authorized by law at the time of issuance. Power Bonds are payable as to both principal and interest solely from Net Power Proceeds but may, at the option of TVA, be paid from the proceeds of refunding obligations or other funds legally available for such payment. Power Bonds are not obligations of, or guaranteed by, the United States of America. Net Power Proceeds for fiscal 1997, 1996, and 1995 were $2.9 billion, $2.9 billion and $2.6 billion, respectively. Power Bonds of each series must be further authorized by Supplemental Resolution.

TVA intends from time to time to issue New Power Bonds with maturities and on terms determined in light of market conditions at the time of sale. The New Power Bonds may be sold to dealers or underwriters, who may resell the New Power Bonds in public offerings or otherwise. In addition, New Power Bonds may be sold by TVA directly or through other entities.

Except for FISBS described below, the specific aggregate principal amount, maturity, interest rate or method for determining such rate, interest payment dates, if any, purchase price to be paid to TVA, any terms for redemption or other special terms, form and denomination of New Power Bonds, information as to any stock exchange listing, and the names of any dealers, underwriters or agents, together with a description of any amendments or supplements to the Basic Resolution in connection with the sale of New Power Bonds being offered at a particular time, will be set forth in an offering circular, and any appropriate supplement thereto, together with the terms of such New Power Bonds.

New Power Bonds include TVA's FISBS that may be issued from time to time in installments with maturities of from one year to fifty years. TVA intends to offer FISBS for sale on a continuous basis to members of a group of securities dealers selected by TVA, who will resell such FISBS. The aggregate principal amount of all such Installment Bonds will not exceed $4 billion at any one time outstanding and the maximum effective rate payable on any such Installment Bonds will not exceed 10 percent.

Information relating to FISBS will be set forth in an Installment Bonds offering circular and any appropriate amendment or supplement thereto. At the time of each sale TVA will determine if the FISBS then being sold will be subject to redemption prior to the maturity date and will establish the purchase price, principal amount, interest rate or interest rate formula, maturity date, and certain other terms of such sale.

TVA's Discount Notes are also issued pursuant to Section 15d of the Act and in accord with Section 2.5 of the Basic Resolution. As of December 31, 1997, TVA had outstanding approximately $2.6 billion in Discount Notes. The Discount Notes are payable solely from Net Power Proceeds (but may, at the option of TVA, be paid from the proceeds of refunding obligations or other funds legally available for such payment) and are not obligations of, or guaranteed by, the United States of America.

TVA intends to offer Discount Notes for sale on a continuous basis to a group of securities dealers selected by TVA, who will resell such notes. Discount Notes will be issued in such form and upon such terms and conditions as deemed appropriate by TVA. Certain information respecting Discount Notes will be set forth in a Discount Notes offering circular and any appropriate supplement thereto.

TVA from time to time may issue Other Indebtedness, in addition to New Power Bonds and Discount Notes, to assist in financing its Power Program. Other Indebtedness, such as Quarterly Income Debt Securities ("QIDS"), are issued pursuant to Section 15d of the Act and under appropriate authorizing resolutions. At December 31, 1997, TVA had outstanding $1.1 billion principal amount of QIDS.

Subordinated debt securities, such as QIDS, may be issued from time to time by TVA with maturities and on terms determined in light of market conditions at the time of sale. These subordinated debt securities may be sold to dealers or underwriters, who may resell them in public offerings or otherwise. In addition, the subordinated debt securities may be sold by TVA directly or through other entities. TVA subordinated debt securities will be payable as to both principal and interest solely from Net Power Proceeds (but may, at the option of TVA, be paid from the proceeds of refunding obligations or other funds legally available for such payment) and will not be obligations of, or guaranteed by, the United States of America.

The specific aggregate principal amount, maturity, interest rate or method for determining such rate, interest payment dates, if any, purchase price to be paid to TVA, any terms for redemption or other special terms, form and denomination of Other Indebtedness, information as to any stock exchange listing, and the names of any dealers, underwriters or agents, will be set forth in an offering circular, and any appropriate supplement thereto, together with the terms of such Other Indebtedness.

The following summary of certain provisions of the Basic Resolution does not purport to be complete and is qualified in its entirety by reference to the full text of the Basic Resolution. See also "Recent Legislation".

Application of Net Power Proceeds

Section 2.3 of the Basic Resolution provides as follows:

> Net Power Proceeds shall be applied, and the Corporation hereby specifically pledges them for application, first to payments due as interest on Bonds, on Bond Anticipation Obligations, and on any Evidences of Indebtedness issued pursuant to Section 2.5 which rank on a parity with Bonds as to interest; to payments of the principal due on Bonds for the payment of which other provisions have not

been made; and to meeting requirements of sinking funds or other analogous funds under any Supplemental Resolutions. The remaining Net Power Proceeds shall be used only for:

(a) Required interest payments on any Evidences of Indebtedness issued pursuant to Section 2.5 which do not rank on a parity with Bonds as to interest.

(b) Required payments of or on account of principal of any Evidences of Indebtedness other than Bonds.

(c) Minimum payments into the United States Treasury required by the Act in repayment of and as a return on the Appropriation Investment.

(d) Investment in Power Assets, additional reductions of the Corporation's capital obligations, and other lawful purposes related to the Power Program; provided, however, that payments into the United States Treasury in any fiscal year in reduction of the Appropriation Investment in addition to the minimum amounts required for such purpose by the Act may be made only if there is a net reduction during such year in the dollar amount of outstanding Evidences of Indebtedness issued for capital purposes, and only to such extent that the percentage of aggregate reduction in the Appropriation Investment during such year does not exceed the percentage of net reduction during the year in the dollar amount of outstanding Evidences of Indebtedness issued for capital purposes.

Section 2.4 of the Basic Resolution provides as follows:

The Corporation, having first adopted a Supplemental Resolution authorizing the issuance of a series of Bonds and pending such issuance, may issue Bond Anticipation Obligations and renewals thereof (including Interim Obligations to the Secretary of the Treasury) to be paid from the proceeds of such series of Bonds when issued or from other funds that may be available for that purpose.

Section 2.5 of the Basic Resolution provides as follows:

To assist in financing its Power Program the Corporation may issue Evidences of Indebtedness other than Bonds and Bond Anticipation Obligations, which may be payable out of Net Power Proceeds subject to the provisions of Section 2.3 hereof, but no such other Evidences of Indebtedness shall rank on a parity with or ahead of the Bonds as to payments on account of the principal thereof or rank ahead of the Bonds as to payments on account of the interest thereon.

See "Amendments to the Basic Resolution to Become Effective in the Future" for a discussion of amendments that will affect the above provisions of Sections 2.3 and 2.5 of the Basic Resolution. See "Recent Legislation" for a discussion of legislation relating to appropriations for TVA's nonpower programs and the funding of such programs, including the use of power revenues.

Rate Covenant

Section 3.2 of the Basic Resolution provides as follows:

The Corporation shall fix, maintain, and collect rates for power sufficient to meet in each fiscal year the requirements of that portion of the present subsection (f) of section 15d of the Act which reads as follows:

> The Corporation shall charge rates for power which will produce gross revenues sufficient to provide funds for operation, maintenance, and administration of its power system; payments to States and counties in lieu of taxes; debt service on outstanding bonds, including provision and maintenance of reserve funds and other funds established in connection therewith; payments to the Treasury as a return on the appropriation investment pursuant to subsection (e) hereof; payment to the Treasury of the repayment sums specified in subsection (e) hereof; and such additional margin as the Board may consider desirable for investment in power system assets, retirement of outstanding bonds in advance of maturity, additional reduction of appropriation investment, and other purposes connected with the Corporation's power business, having due

regard for the primary objectives of the Act, including the objective that power shall be sold at rates as low as are feasible.

For purposes of this Resolution, "debt service on outstanding bonds," as used in the above provision of the Act, shall mean for any fiscal year the sum of all amounts required to be (a) paid during such fiscal year as interest on Evidences of Indebtedness, (b) accumulated in such fiscal year in any sinking or other analogous fund provided for in connection with any Evidences of Indebtedness, and (c) paid in such fiscal year on account of the principal of any Evidences of Indebtedness for the payment of which funds will not be available from sinking or other analogous funds, from the proceeds of refunding issues, or from other sources; provided, however, that for purposes of clause (c) of this definition Bond Anticipation Obligations and renewals thereof shall be deemed to mature in the proportions and at the times provided for paying or setting aside funds for the payment of the principal of the authorized Bonds in anticipation of the issuance of which such Bond Anticipation Obligations were issued.

The rates for power fixed by the Corporation shall also be sufficient so that they would cover all requirements of the above-quoted provision of subsection (f) of section 15d of the Act if, in such requirements, there were substituted for "debt service on outstanding bonds" for any fiscal year the amount which if applied annually for 35 years would retire, with interest at the rates applicable thereto, the originally issued amounts of all series of Bonds and other Evidences of Indebtedness, any part of which was outstanding on October 1 of such year.

Covenant for Protection of Bondholders' Investment

Under the Act and Section 3.3 of the Basic Resolution, TVA must, in each successive 5-year period beginning October 1, 1960, use either for the reduction of its capital obligations (including Evidences of Indebtedness and the Appropriation Investment) or for investment in Power Assets an amount of Net Power Proceeds at least equal to the sum of (1) depreciation accruals and other charges representing the amortization of capital expenditures and (2) the net proceeds from any disposition of power facilities.

Depreciation

The Basic Resolution requires TVA to accrue, in accordance with a recognized method, annual amounts for depreciation of its power properties (except land and other nondepreciable property) which will amortize their original cost less anticipated net salvage value within their expected useful lives. TVA has provided allowances for depreciation of its power properties (except land and other nondepreciable property) on a straight-line basis during their expected useful lives.

Issuance of Additional Bonds and Other Evidences of Indebtedness

The Act presently limits the issuance of Evidences of Indebtedness by TVA to a total of $30 billion outstanding at any one time to assist in financing TVA's power program (and for refunding). At December 31, 1997, TVA had approximately U.S.$26.8 billion and DM 1.5 billion (issued in September 1996) of Evidences of Indebtedness outstanding. The Basic Resolution permits the issuance of Power Bonds only to provide capital for TVA's power program, including the refunding of any Evidences of Indebtedness issued for that purpose.

Power Bonds, the terms and conditions of which may not be inconsistent with the Basic Resolution, must also be authorized by Supplemental Resolution.

The issuance of Power Bonds is limited as follows by the Basic Resolution:

Each Supplemental Resolution authorizing the issuance of Power Bonds must contain a finding by the Board that after the Power Bonds authorized thereby have been issued, Gross Power Revenues will be adequate to meet the requirements of the Basic Resolution with respect to rates and the application of depreciation accruals. These requirements are described under "The Basic Resolution; Power Bonds, Discount Notes and Other Indebtedness" — "Rate Covenant" and — "Covenant for Protection of Bondholders' Investment".

The amount of Power Bonds outstanding may not be increased unless net power income (after interest expense and depreciation charges but before payments as a return on or in reduction of the appropriation investment) for the latest five fiscal years has aggregated at least $200 million. Moreover, that minimum requirement is increased by $15 million for each ¼ percent (or major fraction thereof) by which the average for those five years of the October 1 average interest rate payable by the United States Treasury upon its total marketable public obligations exceeds 3¼ percent. See Section 3.4 of the Basic Resolution and "The Basic Resolution; Power Bonds, Discount Notes and Other Indebtedness" — "Amendments to the Basic Resolution to Become Effective in the Future".

Pending the issuance of Power Bonds authorized by a Supplemental Resolution, Bond Anticipation Obligations and renewals thereof (including Interim Obligations to the Secretary of the Treasury) may be issued, to be paid from the proceeds of such Power Bonds when issued or from other funds that may be available for that purpose.

Evidences of Indebtedness (such as Discount Notes) other than Power Bonds and Bond Anticipation Obligations may also be issued to assist in financing TVA's power program. They may be payable out of Net Power Proceeds subject to the provisions of Section 2.3 of the Basic Resolution. They may not rank on a parity with or ahead of the Power Bonds as to principal or ahead of them as to interest. See "Amendments to the Basic Resolution to Become Effective in the Future".

Mortgaging and Disposal of Power Properties

TVA may not mortgage any part of its power properties and may not dispose of all or any substantial portion of such properties unless provision is made for a continuance of the interest, principal and sinking fund payments due and to become due on all outstanding Evidences of Indebtedness, or for the retirement of such Evidences of Indebtedness.

Modifications of Resolutions and Outstanding Bonds

The Basic Resolution provides for amendments to it, to any Supplemental Resolution, and to any outstanding Power Bonds. In summary, amendments of the respective rights and obligations of TVA and the bondholders may be made with the written consent of the holders of at least 66⅔ percent in principal amount of the outstanding Power Bonds to which the amendment applies; but changes in the maturity, principal amount, redemption premium, or rate of interest or maturity of any interest installment, with respect to any Power Bond, or in the above percentage for any such consent, cannot be made without the consent of the holder of such Power Bonds.

In addition, TVA may amend the Basic Resolution or any Supplemental Resolution without the consent of the bondholders in order (1) to close the Basic Resolution against the issuance of additional Power Bonds or to restrict such issuance by imposing additional conditions or restrictions; (2) to add other covenants and agreements to be observed by TVA or to eliminate any right, power or privilege conferred upon TVA by the Basic Resolution; (3) to modify any provisions to release TVA from any of its obligations, covenants, agreements, limitations, conditions or restrictions, provided that such modification or release shall not become effective with respect to any Power Bonds issued prior to the adoption of such amendment; (4) to correct any defect, ambiguity or inconsistency in, or to make provisions in regard to matters or questions arising under, the Basic Resolution or any Supplemental Resolution, so long as such amendments are not contrary to, or inconsistent with, the Basic Resolution or such Supplemental Resolution; or (5) to make any other modification or amendment which the Board by resolution determines will not materially and adversely affect the interests of holders of the Power Bonds.

Events of Default

Any of the following shall be deemed an Event of Default under the Basic Resolution: (i) default in the payment of the principal or redemption price of any Power Bond when due and payable at maturity, by call for redemption, or otherwise; (ii) default in the payment of any installment of interest on any Power Bond when due and payable for more than 30 days; or (iii) failure of TVA to duly perform any other covenant, condition or agreement contained in the Power Bonds or in the Basic Resolution or any Supplemental Resolution for 90 days after written notice specifying such failure has been given to TVA by the holders of at least 5 percent in aggregate principal amount of the then outstanding Power Bonds.

Upon any such Event of Default, the holders of the Power Bonds may proceed to protect and enforce their respective rights, subject to the restrictions described below. The holders of at least 5 percent in aggregate principal amount of Power Bonds then outstanding shall, subject to certain restrictions, have the right and power to institute a proceeding (i) to enforce TVA's covenants and agreements, (ii) to enjoin any acts in violation of the rights of holders of Power Bonds, and (iii) to protect and enforce the rights of holders of Power Bonds. Power Bonds do not provide for acceleration upon an Event of Default.

Such holders have no right to bring any such action or proceeding against TVA unless they have given TVA written notice of an Event of Default, and TVA has had a reasonable opportunity to take appropriate corrective action with respect thereto and has failed or refused to do so.

Holders of a majority in aggregate principal amount of the outstanding Power Bonds have the right to direct the time, method and place of conducting any proceeding for any remedy available and may waive any default and its consequences, except a default in the payment of the principal of, premium, if any, or interest on any Power Bonds.

Amendments to the Basic Resolution to Become Effective in the Future

On March 25, 1992, TVA adopted a resolution amending the Basic Resolution, entitled "Fourth Amendatory Resolution to Basic Tennessee Valley Authority Power Bond Resolution" (the "Fourth Amendatory Resolution"). The amendments to the Basic Resolution made by the Fourth Amendatory Resolution will become effective only at such time as either (a) all Power Bonds issued prior to the date of adoption of the Fourth Amendatory Resolution cease to be outstanding (which will occur not later than November 15, 2029) or (b) the holders of at least 66⅔ percent of the principal amount of all then outstanding Power Bonds issued prior to the adoption of the Fourth Amendatory Resolution consent in writing to such amendments. At such times as the amendments become effective, they shall apply to all Power Bonds. The holders of Power Bonds offered after March 25, 1992, shall be deemed to have given their consent to the effect that, at any time after the conditions set forth in (a) or (b) above have been met, the amendments to the Basic Resolution made by the Fourth Amendatory Resolution will become effective in the manner provided. No further vote or consent of the holders of Power Bonds offered after March 25, 1992, is required to permit such amendments to the Basic Resolution to become effective.

The Fourth Amendatory Resolution, when effective in accordance with its terms and the terms of the Basic Resolution as described above, will (1) delete from the Basic Resolution the limitation on issuance of Power Bonds set forth in Section 3.4 thereof and (2) amend the Basic Resolution to permit issuance of other Evidences of Indebtedness under Section 2.5 thereof that rank on a parity with Power Bonds as to principal and interest.

Section 3.4 of the Basic Resolution presently restricts TVA's ability to issue Power Bonds unless net power income (after interest expense and depreciation charges but before payments as a return on or in reduction of the Appropriation Investment) for the latest five fiscal years has aggregated at least $200 million. That amount is increased by $15 million for each ¼ percent (or major fraction thereof) by which the average for those five years of the October 1 average interest rates payable by the United States Treasury upon its total marketable public obligations exceeds 3¼ percent. Upon the effectiveness of the Fourth Amendatory Resolution (which eliminates Section 3.4) Sections 3.5 through 3.10 will be renumbered as appropriate.

The foregoing is a brief summary of certain provisions of the Fourth Amendatory Resolution. This summary is not to be considered a full statement of the terms of the Fourth Amendatory Resolution and, accordingly, is qualified by reference to the Fourth Amendatory Resolution. Copies in reasonable quantity of the Fourth Amendatory Resolution may be obtained upon written request directed to Tennessee Valley Authority, 400 West Summit Hill Drive, Knoxville, Tennessee 37902, Attention: Vice President and Treasurer, or by calling (423) 632-3366.

Recent Legislation

In October 1997, Congress enacted the Energy and Water Development Appropriations Act, 1998, Pub. L. No. 105-62, 111 Stat. 1320, 1338 (1997). The paragraph captioned "TENNESSEE VALLEY AUTHORITY" in Title IV of this act (such paragraph being hereinafter referred to as the "Appropriations Act paragraph") (1) appropriates $70 million for TVA's nonpower programs in fiscal year 1998; (2) anticipates no further appropriations to TVA thereafter; and (3) requires TVA, beginning with October 1, 1998, to fund nonpower programs that constitute "essential stewardship activities" with revenues derived from one or more of various sources, including power revenues, notwithstanding provisions of the TVA Act and power bond covenants to the contrary. TVA has not yet made determinations as to funding its nonpower activities after September 30, 1998.

The Appropriations Act paragraph states;

> For the purpose of carrying out the provisions of the Tennessee Valley Authority Act of 1933, as amended (16 U.S.C. ch. 12A), including hire, maintenance, and operation of aircraft, and purchase and hire of passenger motor vehicles, $70,000,000, to remain available until expended, of which $6,900,000 shall be available for operation, maintenance, surveillance, and improvement of Land Between the Lakes; and for essential stewardship activities for which appropriations were provided to the Tennessee Valley Authority in Public Law 104-206, such sums as are necessary in fiscal year 1999 and thereafter, to be derived only from one or more of the following sources: nonpower fund balances and collections; investment returns of the nonpower program; applied programmatic savings in the power and nonpower programs; savings from the suspension of bonuses and awards; savings from reductions in memberships and contributions; increases in collections resulting from nonpower activities, including user fees; or increases in charges to private and public utilities both investor and cooperatively owned, as well as to direct load customers: *Provided,* That such funds are available to fund the stewardship activities under this paragraph, notwithstanding sections 11, 14, 15, 29, or other provisions of the Tennessee Valley Authority Act, as amended, or provisions of the TVA power bond covenants: *Provided further,* That the savings from, and revenue adjustments to, the TVA budget in fiscal year 1999 and thereafter shall be sufficient to fund the aforementioned stewardship activities such that the net spending authority and resulting outlays for these activities shall not exceed $0 in fiscal year 1999 and thereafter.

However, the Clinton administration's proposed budget for fiscal year 1999 includes $76.8 million for TVA's nonpower programs. TVA cannot predict whether Congress will approve this amount or otherwise appropriate funds for TVA's nonpower programs in fiscal year 1999 or thereafter.

In 1997 three other bills were introduced in Congress which, beginning with fiscal years 1998 to 2001, would eliminate the provision in the TVA Act permanently authorizing appropriations for TVA. TVA does not anticipate enactment of any of these three bills.

Stripping

Certain series of the Corporation's New Power Bonds (the "Eligible New Power Bonds") may be separated ("stripped") into their Interest and Principal Components (as hereinafter defined) and maintained as such on the book-entry records of the Federal Reserve Banks. The components of each Eligible New Power Bond are: each future interest payment due on or prior to the first date on which the Eligible New Power Bond is subject to redemption at the option of the Corporation (each an "Interest Component"); and the principal payment plus any interest payments after the first date on which the Eligible New Power Bond is subject to redemption at the option of the Corporation (the "Principal Component"). Each Interest Component and the Principal Component will receive an identifying designation and CUSIP number. A request for separation of an Eligible New Power Bond into its Interest and Principal Components must be made to the Federal Reserve Bank of New York ("FRBNY"). Currently the FRBNY does not charge a fee for stripping Eligible New Power Bonds. For an Eligible New Power Bond to be stripped into its Interest and Principal Components as described above, the principal amount of the Eligible New Power Bond must be in an amount that, based on the stated interest rate of the Eligible New Power Bonds, will produce a semi-annual interest payment of $1,000 or multiples thereof. The minimum principal amounts required to strip an Eligible New Power Bond at various interest rates, as well as the interest payments corresponding to those minimum principal amounts, may be obtained by calling the Corporation's Vice President and Treasurer at (423) 632-3366, and the minimum principal amount required to strip an Eligible New Power Bond will be disclosed in a related offering circular except for Installment Bonds. Interest and Principal Components will be obligations of TVA payable solely from TVA's Net Power Proceeds.

Once a New Power Bond has been stripped into its Interest and Principal Components, the Interest and Principal Components may be maintained and transferred on the book-entry system of the Federal Reserve Banks in integral multiples of $1,000. Payments on the Interest and Principal Components will be made on the applicable payment dates on the related New Power Bonds by crediting holders' accounts at the FRBNY. At the request of a holder and on the holder's payment of a fee (currently the FRBNY's fee applicable to on-line book-entry securities transfers), the FRBNY will restore ("reconstitute") the unmatured Interest and Principal Components of a stripped New Power Bond to their fully constituted form. Holders wishing to reconstitute the unmatured Interest and Principal Components of a stripped New Power Bond to their fully constituted form must (i) produce all outstanding Interest and Principal Components for a stripped New Power Bond and (ii) comply with all applicable requirements of the FRBNY governing the stripping and reconstitution of securities.

The offering price of the Interest and Principal Components could be at substantial discounts from their face amounts and, as a result, these components may be subject to greater interest rate volatility than the fully constituted New Power Bonds or other obligations bearing current interest. There also may be a less liquid secondary market for such Interest and Principal Components as compared to the secondary market for the fully constituted New Power Bonds.

The Interest and Principal Components of Eligible New Power Bonds could be subject to restrictions or requirements with respect to the legality of investment therein which do not apply to New Power Bonds held in their fully constituted form. Thus, each person or entity is advised to consult with its own counsel with respect to the legality of investment in Interest and Principal Components.

INDEPENDENT ACCOUNTANTS

The financial statements of TVA at September 30, 1997, and 1996 and for each of the three fiscal years in the period ended September 30, 1997, appended hereto as part of this Information Statement, have been audited by Coopers & Lybrand L.L.P., independent accountants, as set forth in their report, dated October 23, 1997, which report is also appended hereto.

* * * * *

Any statements in this Information Statement involving matters of opinion, whether or not expressly so stated, are intended as such and not as representations of fact. This Information Statement is not to be construed as a contract or agreement with the purchaser of any of the New Power Bonds, Discount Notes or Other Indebtedness.

This Information Statement has been approved by a duly authorized officer of the Tennessee Valley Authority.

Tennessee Valley Authority

By: /s/ JOHN M. HOSKINS

John M. Hoskins
Vice President and
Treasurer

Dated February 27, 1998

TENNESSEE VALLEY AUTHORITY

FINANCIAL STATEMENTS

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TENNESSEE VALLEY AUTHORITY

BALANCE SHEETS
At September 30, 1997 and 1996

	Power program 1997	Power program 1996	All programs 1997	All programs 1996
	(in millions)			
ASSETS				
Current Assets				
Cash and cash equivalents	$ 299	$ 238	$ 374	$ 318
Accounts receivable	701	680	707	689
Inventories at average cost and other				
Fuel	112	110	112	110
Other	287	278	287	278
Total current assets	1,399	1,306	1,480	1,395
Property, Plant and Equipment				
Completed plant	28,528	27,955	29,632	29,069
Less accumulated depreciation	(7,178)	(6,553)	(7,469)	(6,854)
Net completed plant	21,350	21,402	22,163	22,215
Construction in progress	605	744	622	764
Deferred nuclear generating units	6,303	6,293	6,303	6,293
Nuclear fuel and capital leases	1,040	1,082	1,040	1,082
Total property, plant and equipment	29,298	29,521	30,128	30,354
Investment Funds	561	440	561	440
Deferred Charges and Other Assets				
Loans and other long-term receivables	121	319	170	375
Debt issue and reacquisition costs	1,096	1,162	1,096	1,162
Other deferred charges	1,209	1,281	1,209	1,281
Total deferred charges and other assets	2,426	2,762	2,475	2,818
Total assets	$33,684	$34,029	$34,644	$35,007
LIABILITIES AND PROPRIETARY CAPITAL				
Current Liabilities				
Accounts payable	$ 468	$ 392	$ 487	$ 417
Accrued liabilities	161	187	172	196
Accrued interest	499	498	499	498
Discount notes	2,151	1,774	2,151	1,774
Current maturities of long-term debt	574	2,250	574	2,250
Total current liabilities	3,853	5,101	3,883	5,135
Other Liabilities	1,704	1,580	1,704	1,580
Long-term Debt				
Public bonds — senior	20,354	19,403	20,354	19,403
Federal Financing Bank — senior	3,200	3,200	3,200	3,200
Public bonds — subordinated	1,100	1,100	1,100	1,100
Unamortized discount and other adjustments	(502)	(383)	(502)	(383)
Total long-term debt	24,152	23,320	24,152	23,320
Proprietary Capital				
Appropriation investment	588	608	4,887	4,800
Retained earnings reinvested in power program	3,387	3,420	3,387	3,420
Accumulated net expense of nonpower programs	—	—	(3,369)	(3,248)
Total proprietary capital	3,975	4,028	4,905	4,972
Total liabilities and proprietary capital	$33,684	$34,029	$34,644	$35,007

The accompanying notes are an integral part of these financial statements.

TENNESSEE VALLEY AUTHORITY

STATEMENTS OF INCOME — POWER PROGRAM
For the Years Ended September 30, 1997, 1996 and 1995

	1997	1996 (in millions)	1995
Operating Revenues			
Sales of electricity			
Municipalities and cooperatives	$4,811	$4,980	$4,654
Industries directly served	464	452	460
Federal agencies	179	172	179
Other	98	89	82
Total operating revenues	5,552	5,693	5,375
Operating Expenses			
Fuel and purchased power, net	1,211	1,278	1,443
Operating and maintenance	1,201	1,218	1,050
Depreciation and amortization	1,014	904	703
Tax-equivalents	272	256	252
Total operating expenses	3,698	3,656	3,448
Operating income	1,854	2,037	1,927
Other Income (Expense), Net	157	(10)	(91)
Income before interest expense	2,011	2,027	1,836
Interest Expense			
Interest on debt	1,993	1,965	1,908
Amortization of debt discount, issue, and reacquisition costs, net	91	118	116
Allowance for funds used during construction	(81)	(117)	(198)
Net interest expense	2,003	1,966	1,826
Net Income	$ 8	$ 61	$ 10

The accompanying notes are an integral part of these financial statements.

TENNESSEE VALLEY AUTHORITY

STATEMENTS OF CASH FLOWS
For the Years Ended September 30, 1997, 1996, and 1995

	Power program			All programs		
	1997	1996	1995	1997	1996	1995
	(in millions)					
Cash Flows From Operating Activities						
Net power income	$ 8	$ 61	$ 10	$ 8	$ 61	$ 10
Net expense of nonpower programs	—	—	—	(121)	(127)	(182)
Items not requiring (providing) cash						
Depreciation and amortization	1,066	924	715	1,080	938	728
Allowance for funds used during construction	(81)	(117)	(198)	(81)	(117)	(198)
Nuclear fuel amortization	196	156	112	196	156	112
Other, net	(151)	162	72	(151)	164	142
Changes in current assets and liabilities						
Accounts receivable	(24)	(1)	(5)	(21)	7	22
Inventories and other	(19)	(22)	(8)	(19)	(22)	(8)
Accounts payable and accrued liabilities	56	(246)	74	52	(250)	(36)
Accrued interest	1	43	31	1	43	31
Other	14	(50)	(1)	14	(50)	(2)
Net cash provided by operating activities	1,066	910	802	958	803	619
Cash Flows From Investing Activities						
Construction expenditures	(722)	(1,107)	(1,868)	(733)	(1,121)	(1,880)
Allowance for funds used during construction	81	117	198	81	117	198
Nuclear fuel	(159)	(76)	(77)	(159)	(76)	(77)
Proceeds from sale of investments	513	(162)	(100)	513	(162)	(100)
Purchases of investments	(483)	—	—	(483)	—	—
Proceeds from sale of loans receivable	211	—	—	211	—	—
Other, net	(21)	(26)	(24)	(13)	(13)	(39)
Net cash used in investing activities	(580)	(1,254)	(1,871)	(583)	(1,255)	(1,898)
Cash Flows From Financing Activities						
Long-term debt						
Issues	3,100	4,400	3,500	3,100	4,400	3,500
Redemptions	(3,829)	(2,706)	(2,503)	(3,829)	(2,706)	(2,503)
Short-term borrowings, net	377	(1,057)	222	377	(1,057)	222
Borrowing expenses, net	(12)	(44)	(38)	(12)	(44)	(38)
Congressional appropriations	—	—	—	106	109	139
Payments to U.S. Treasury	(61)	(63)	(62)	(61)	(63)	(62)
Net cash (used in) provided by financing activities	(425)	530	1,119	(319)	639	1,258
Net change in cash and cash equivalents	61	186	50	56	187	(21)
Cash at beginning of period	238	52	2	318	131	152
Cash at end of period	$ 299	$ 238	$ 52	$ 374	$ 318	$ 131

The accompanying notes are an integral part of these financial statements.

TENNESSEE VALLEY AUTHORITY

STATEMENTS OF CHANGES IN PROPRIETARY CAPITAL — POWER PROGRAM

	For the years ended September 30,		
	1997	1996	1995
		(in millions)	
Retained earnings reinvested at beginning of period	$3,420	$3,402	$3,434
Net income	8	61	10
Return on appropriation investment	(41)	(43)	(42)
Retained earnings reinvested at end of period	3,387	3,420	3,402
Appropriation investment at beginning of period	608	628	648
Return of appropriation investment	(20)	(20)	(20)
Appropriation investment at end of period	588	608	628
Proprietary capital at end of period	$3,975	$4,028	$4,030

STATEMENTS OF NET EXPENSE — NONPOWER PROGRAMS

	For the years ended September 30,		
	1997	1996	1995
		(in millions)	
Water and Land Stewardship	$ 78	$ 75	$ 63
Land Between The Lakes	7	7	6
Economic Development	22	25	23
Environmental Research Center	14	20	21
Columbia Dam	—	—	69
Net expense	$121	$127	$182

STATEMENTS OF CHANGES IN PROPRIETARY CAPITAL — NONPOWER PROGRAMS

	For the years ended September 30,		
	1997	1996	1995
		(in millions)	
Proprietary capital at beginning of period	$944	$ 964	$1,007
Congressional appropriations	106	109	139
Net expense	(121)	(127)	(182)
Other, net	1	(2)	—
Proprietary capital at end of period	$930	$ 944	$ 964

The accompanying notes are an integral part of these financial statements.

TENNESSEE VALLEY AUTHORITY

NOTES TO FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

General

TVA is a wholly-owned corporate agency and instrumentality of the United States. It was established by the TVA Act with the objective of developing the resources of the Tennessee Valley region in order to strengthen the regional and national economy and the national defense by providing: (1) an ample supply of power within the region, (2) navigable channels and flood control for the Tennessee River System, and (3) agricultural and industrial development and improved forestry in the region. TVA carries out these regional and national responsibilities in a service area that centers on Tennessee and parts of Alabama, Georgia, Kentucky, Mississippi, North Carolina and Virginia.

TVA's programs are divided into two types of activities — the power program and the non-power programs. Substantially all TVA revenues and assets are attributable to the power program. The power program is separate and distinct from the non-power programs and is required to be self-supporting from power revenues and funds borrowed from public markets. The power program receives no congressional appropriations and is required to make annual payments to the U.S. Treasury in repayment of, and as a return on, the government's appropriation investment in TVA power facilities. Most of the funding for TVA's non-power programs has been provided by congressional appropriations. Certain nonpower activities are also funded by various revenues and user fees. Financial accounts for the power and non-power programs are kept separately.

Power rates are established by the TVA Board of Directors as authorized by the TVA Act. The TVA Act requires TVA to charge rates for power that, among other things, will produce gross revenues sufficient to provide funds for operation, maintenance and administration of its power system; payments to states in lieu of taxes; and debt service on outstanding indebtedness.

Fiscal year

Unless otherwise indicated, years (1997, 1996, etc.) refer to TVA's fiscal years ended September 30.

Revenue recognition

Revenues from power sales are recorded as service is rendered to customers. TVA accrues estimated unbilled revenues for power sales provided to customers for the period of time from the end of the billing cycle to month-end.

Property, plant, and equipment, and depreciation

Additions to plant are recorded at cost, which includes direct and indirect costs such as general engineering, a portion of corporate overhead and an allowance for funds used during construction. The cost of current repairs and minor replacements is charged to operating expense. The TVA Act requires TVA's Board of Directors to allocate the cost of completed multi-purpose projects between the power and nonpower programs, subject to the approval of the President of the United States. The original cost of property retired, together with removal costs less salvage value, is charged to accumulated depreciation. Depreciation is generally computed on a straight-line basis over the estimated service lives of the various classes of assets. Depreciation expense expressed as a percentage of the average annual depreciable completed plant was 3.21 percent for 1997 and 1996 and 3.35 percent for 1995.

Decommissioning costs

During 1997 the excess of decommissioning investment earnings over the annual decommissioning provision was recorded as other income. Of the total investment earnings of $151 million, $13 million was recorded as an offset to the decommissioning provision, with the $138 million excess recorded as other income. During 1996 the annual decommissioning provision of $30 million exceeded the earnings from decommissioning fund investments of $17 million and the $13 million excess was charged to depreciation expense. During 1995, investment earnings approximated decommissioning expense and no decommissioning charges were made to depreciation expense.

Allowance for funds used during construction

The practice of capitalizing an allowance for funds used during construction is followed in the power program. The allowance is applicable to construction in progress excluding deferred nuclear generating units. In 1995, TVA changed its assumptions used in determining the interest rate used to calculate the allowance for funds used during construction. The change was made to more accurately reflect the nature of the indebtedness issued to fund construction. The effect of the change for 1995 was to increase the amount of interest capitalized by approximately $56 million.

Loans and other long-term receivables

In June 1997, TVA entered into a five-year agreement with a bank pursuant to which TVA agreed to sell certain receivables relating to TVA's consumer energy-conservation programs. As of September 30, 1997, a $211-million pool had been sold for proceeds equal to its carrying amount. In accordance with Statement of Financial Accounting Standards (SFAS) No. 125, *Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities*, the transaction has been reflected as a reduction of loans and other long-term receivables. Under the terms of the agreement, TVA has retained substantially the same risk of credit loss as if the receivables had not been sold and, accordingly, an appropriate liability account has been retained.

Other deferred charges

Deferred charges primarily include prepaid pension costs and regulatory assets capitalized under the provisions of SFAS No. 71, *Accounting for the Effects of Certain Types of Regulation*. At September 30, 1997, other deferred charges included total unamortized regulatory assets of $950 million — of which $468 million represents a capitalized interest component of nuclear fuel; $411 million represents a transition obligation related to the adoption of SFAS No. 112, *Employers Accounting for Postemployment Benefits*; and $71 million represents TVA's portion of the costs for decommissioning the Department of Energy's nuclear waste disposal facility. At September 30, 1996, the unamortized balances of these three regulatory assets were $595 million, $446 million and $81 million, respectively, for a total of $1,122 million. These regulatory assets are being amortized over periods ranging from eight to 15 years, generally on a straight-line basis.

Investment funds

Investment funds consist primarily of a portfolio of investments in trusts designated for funding nuclear decommissioning requirements (see note 10). These funds, at September 30, 1997, were invested in portfolios generally designed to earn returns in line with overall equity market performance.

Debt issue and reacquisition costs

Issue and reacquisition expenses, call premiums and other related costs are deferred and amortized (accreted), respectively, on a straight-line basis over the term of the related outstanding securities.

TVA has also incurred premiums related to certain advanced refundings. In accordance with regulatory practices, TVA has deferred these premiums and is amortizing them to expense ratably through the maturity dates of the new debt issues. The unamortized balances of such regulatory assets at September 30, 1997 and 1996, were $983 million and $1,042 million, respectively.

Tax-equivalents

The TVA Act requires TVA to make payments to states and local governments in which the power operations of the corporation are conducted. The basic amount is 5 percent of gross revenues from the sale of power to other than federal agencies during the preceding year, with the provision for minimum payments under certain circumstances. Cash paid for tax-equivalents for 1997, 1996 and 1995 have been $272 million, $256 million and $252 million, respectively.

Interest and capital costs

During 1997, 1996 and 1995, cash paid for interest on outstanding indebtedness (net of amount capitalized) was $1,911 million, $1,805 million and $1,678 million, respectively. In addition to paying interest on outstanding indebtedness, the TVA Act requires TVA to make annual payments to the U.S. Treasury. The annual Treasury payments represent a repayment of the original appropriation investment, along with a return on the appropriation investment. TVA paid $20 million each year for 1997, 1996 and 1995 as a repayment of the appropriation investment. TVA paid $41 million to the U.S. Treasury in 1997 as a return on the appropriation investment, while paying $43 million in 1996 and $42 million in 1995.

Risk-management activities

TVA is exposed to market risk from changes in interest rates and currency exchange rates. To manage volatility relating to these exposures, TVA has entered into various derivative transactions, principally interest rate swap agreements and foreign currency swap contracts. TVA is exposed to credit losses in the event of nonperformance by counterparties on the risk-management instruments. TVA monitors such risk and does not believe that there is a significant risk of nonperformance by any of the parties of these instruments.

Statements of cash flows

Cash and cash equivalents include the cash available in commercial bank accounts and U.S. Treasury accounts, as well as short-term securities held for the primary purpose of general liquidity. Such securities mature within three months from the date of acquisition.

Research and development costs

Expenditures related to research and development costs of new or existing products and processes are expensed as incurred. The amounts charged against income were $44 million in 1997, $45 million in 1996 and $43 million in 1995.

Insurance

TVA is primarily self-insured for property loss, workers' compensation, general liability and automotive liability. TVA is also self-insured for health care claims for eligible active and retired employees. Consulting actuaries assist TVA in determining its liability for self-insured claims. TVA maintains nuclear liability insurance with an outside party (see note 10).

Management estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the related amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

2. NUCLEAR POWER PROGRAM

The nuclear power program at September 30, 1997, consisted of nine units — five operating, three deferred, and one inoperative — at four locations, with investments in property, plant and equipment as follows and in the status indicated:

	Operating units	Installed capacity (megawatts)	Completed plant, net	Construction in progress	Deferred	Fuel investment
			(in millions)			
Browns Ferry	2	2,304	$ 3,508	$ 44	$ —	$289
Sequoyah	2	2,442	2,055	77	—	146
Watts Bar	1	1,270	6,674	34	1,716	108
Bellefonte	—	—	—	—	4,587	—
Raw materials			—	—	—	297
Total	5	6,016	$12,237	$155	$6,303	$840

Browns Ferry 3, taken off-line in March 1985 for plant modifications and regulatory improvements, was returned to service in 1996. Browns Ferry 1, also taken off-line in 1985 for modifications and improvements, will continue to remain in an inoperative status until its ultimate disposition is determined. For financial reporting purposes, the undepreciated cost of Browns Ferry 1 of $80 million is included in net completed plant and is being depreciated as part of the recoverable cost of the plant over the remaining license period.

Watts Bar 1 began operating commercially during 1996. In 1988, TVA suspended construction activities on Watts Bar 2 and the unit is currently in lay-up. Bellefonte 1 and 2 were deferred in 1988 and 1985, respectively. Estimated 1998 expenditures for the three deferred units total $9 million and are limited to lay-up, maintenance and ensuring that options remain viable.

In 1993, TVA began an integrated resource planning process to determine TVA's strategy for meeting future customer energy demands. As part of this long-term energy strategy, TVA re-evaluated the need for finishing Bellefonte 1 and 2 and Watts Bar 2 as nuclear units. In December 1994, TVA determined it will not, by itself, complete Bellefonte 1 and 2 and Watts Bar 2 as nuclear units. In the Integrated Resource Plan (IRP), TVA determined that it would study the potential for converting the Bellefonte Nuclear Plant to a combined cycle plant utilizing natural gas or gasified coal as the primary fuel and/or joint venturing with a partner for completion. The feasibility of converting Bellefonte to such an alternative fuel will require will require in-depth engineering and financial analyses; and accordingly, TVA is utilizing a team of technical and financial experts. The IRP also concluded that Watts Bar 2 should remain in deferred status until completion of the Bellefonte study. The impact on TVA's financial position of completing, converting or joint venturing these units will be determined upon completion of the Bellefonte study. The future decisions on these units will ultimately impact the method of cost recovery, and the TVA Board has determined that it will, at that time, establish rate adjustments and operating policies to ensure full recovery of the cost of these units and compliance with the requirements of the TVA Act. For financial reporting purposes, the cost of the three units is presented as deferred nuclear generating units.

3. COMPLETED PLANT

Completed plant consists of the following at September 30:

	1997			1996		
Power program	Cost	Accumulated depreciation	Net	Cost	Accumulated depreciation	Net
			(in millions)			
Fossil plants	$ 7,427	$2,954	$ 4,473	$ 7,320	$2,790	$ 4,530
Nuclear plants	14,514	2,277	12,237	14,370	1,835	12,535
Transmission	3,144	982	2,162	2,911	943	1,968
Hydro plants	1,382	471	911	1,273	454	819
Other	2,061	494	1,567	2,081	531	1,550
Total power	$28,528	$7,178	$21,350	$27,955	$6,553	$21,402

4. LEASES

Certain property, plant and equipment are leased under agreements with terms ranging from one to 30 years. Most of the agreements include purchase options or renewal options that cover substantially all the economic lives of the properties. Obligations under capital lease agreements in effect as September 30 were:

Fiscal year	General plant capital leases
	(in millions)
1998	$ 36
1999	36
2000	36
2001	36
2002	36
Thereafter	301
Total future minimum lease payments	481
Less interest element	(280)
Present value of future minimum lease payments	$ 201

5. APPROPRIATION INVESTMENT — POWER PROGRAM

The TVA Act requires TVA to make annual payments to the U.S. Treasury from net power proceeds. The payments required by the TVA Act may be deferred under certain circumstance for not more than two years. The return is based on the appropriation investment as of the beginning of the year and the computed average interest rate payable by the U.S. Treasury on its total marketable public obligations as of the same date (6.71 percent at September 30, 1997).

6. DEBT

Borrowing authority

The TVA Act authorizes TVA to issue bonds, notes and other evidences of indebtedness up to a total of $30 billion outstanding at any one time. TVA must meet certain cash flow and earnings tests that are contained in the TVA Act and the Basic TVA Power Bond Resolution. Debt service on these obligations, which is payable solely from TVA's net power proceeds, has precedence over the payment to the U.S. Treasury described in note 5.

Debt outstanding

Debt outstanding at September 30, 1997 and 1996 (excluding defeased debt of $950 million at September 30, 1996, which is not considered by TVA to be debt that is subject to the $30 billion bond limit), consisted of the following:

	1997	1996
	(in millions)	
Short-term debt		
Held by the public		
Discount notes (net of discount)	$ 2,151	$ 1,774
Current maturities of long-term debt — 5.07% to 5.98%	574	2,250
Total short-term debt	2,725	4,024
Long-term debt		
Held by the public — senior		
Maturing in 1998	—	1,453
Maturing in 1999 — 5.88% to 6.58%	2,450	750
Maturing in 2000 — 8.375%	1,000	1,000
Maturing in 2001 — 6.00% to 6.50%	1,800	1,250
Maturing in years 2002 through 2045 — 6.125% to 8.625%	15,104	14,950
Held by Federal Financing Bank — senior		
Maturing in 2003 through 2016 — 8.535% to 11.695%	3,200	3,200
Held by the public — subordinated		
Maturing in 2045 through 2046 — 7.50% to 8.00%	1,100	1,100
Total long-term debt	24,654	23,703
Unamortized discount and other adjustments	(502)	(383)
Net long-term debt	24,152	23,320
Total debt	$26,877	$27,344

Short-term debt

The weighted average rates applicable to short-term debt outstanding in the public market as of September 30, 1997 and 1996, were 5.56 percent and 5.38 percent, respectively. During 1997, 1996 and 1995, the maximum outstanding balance of short-term borrowings held by the public was (in millions) $3,962, $3,537 and $3,503 respectively, and the average amounts (and weighted average interest rates) of such borrowings were approximately (in millions), $2,743 (5.47 percent), $2,692 (5.50 percent) and $2,743 (5.83 percent), respectively.

Put and call options

Bond issues of $12.8 billion held by the public are redeemable in whole or in part, at TVA's option, on call dates ranging from the present to April 2012 at call prices ranging from 100 percent to 106.7 percent of the principal amount. Additionally, TVA has bond issues of $2.1 billion held by the public that are redeemable in whole or in part at the option of the respective bondholders. One bond issue totaling $500 million, which matures in July 2045, is redeemable in 2001 by the bondholders. A second issue totaling $121.3 million, which matures in April 2036, is redeemable in 1998 or 2006 at the option of the bondholders and a third issue totaling $1.5 billion, which matures in April 2036, is redeemable in 1999 or 2006 at the option of the bondholders. All of these issues are reported in the debt schedule with maturity dates corresponding to the earliest redeemable dates.

Subsequent to September 30, 1997, TVA monetized the call provisions on approximately $1 billion of public bond issues. The premium received by TVA has been deferred and is being amortized over the term of the agreements.

Bond discount and premium

Discounts and premiums on power borrowings are deferred and amortized (accreted), respectively, as components of interest expense on a straight-line basis over the term of the related outstanding securities.

Foreign currency transaction and interest rate swap

During 1996, TVA entered into a currency swap contract as a hedge for a foreign currency denominated debt transaction where TVA issued 1.5 billion Deutschemark bonds, the cash flows of which were swapped for those of a U.S. dollar obligation of $1 billion. Any gain (loss) on the debt instrument due to the foreign currency transaction is offset by a loss (gain) on the swap contract. At September 30, 1997 and 1996 the currency transaction resulted in gains of $131 million and $16 million, respectively, which are included in the account "unamortized discount and other adjustments." The offsetting loss on the swap contract is recorded as a deferred liability. If any loss/gain were to be incurred as a result of the early termination of the swap contract, any resulting charge (income) would be amortized over the remaining life of the bond as a component of interest expense.

Additionally, TVA entered into a 10-year fixed rate interest swap agreement with a notional amount of $300 million. Such agreement was entered into to hedge TVA's inflation exposure related to its inflation-indexed accreting principal bonds.

7. FAIR VALUE OF FINANCIAL INSTRUMENTS

TVA uses the methods and assumptions described below to estimate the fair values of each significant class of financial instrument.

Cash and cash equivalents, and short-term debt

The carrying amount approximates fair value because of the short-term maturity of these instruments.

Investment funds

At September 30, 1997, these investments were classified as trading securities and carried at their fair value.

Loans and other long-term receivables

Fair values for these homogenous categories of loans and receivables are estimated by determining the present value of future cash flows using the current rates at which similar loans are presently made to borrowers with similar credit ratings and for the same remaining maturities.

Bonds

Fair value of long-term debt traded in the public market is determined by multiplying the par value of the bonds by the quoted market price (asked price) nearest the balance sheet date. The fair value of other long-term debt and long-term debt held by the Federal Financing Bank is estimated by determining the present value of future cash flows using rates of financial instruments with quoted market prices of similar characteristics and the same remaining maturities.

The estimated values of TVA's financial instruments at September 30 are as follows:

	1997		1996	
	Carrying amount	Fair amount	Carrying amount	Fair amount
	(in millions)			
Cash and cash equivalents	$ 374	$ 374	$ 318	$ 318
Investment funds	561	561	440	440
Loans and other long-term receivables	170	160	375	365
Short-term debt	2,151	2,151	1,774	1,774
Long-term debt, including current maturities	25,228	26,127	25,953	26,562

The fair market value of the financial instruments held at September 30, 1997 may not be representative of the actual gains or losses that will be recorded when these instruments mature or if they are called or presented for early redemption.

8. BENEFIT PLANS

Pension plan

TVA has a defined benefit plan for most full-time employees that provides two benefit structures, the Original Benefit Structure and the Cash Balance Benefit Structure. The plan assets are primarily stocks and bonds. TVA contributes to the plan such amounts as are agreed upon between TVA and the TVA Retirement System board of directors, which in no event would be less than the amount necessary on an actuarial basis to provide assets sufficient to meet obligations for benefits. The pension benefit for participants in the Original Benefit Structure is based on the member's years of creditable service, average base pay for the highest three consecutive years and the pension rate for the member's age and years of service, less a Social Security offset.

The Cash Balance Benefit Structure was implemented January 1, 1996. The pension benefit for participants in the Cash Balance Benefit Structure is based on credits accumulated in the member's account and member's age. A member's account receives credits each pay period equal to 6 percent of his or her straight-time earnings. The account also increases at an interest rate equal to the change in the Consumer Price Index plus 3 percent, which amounted to 5.82 percent for both 1997 and 1996. The components of pension expense for the years ended September 30 were:

	1997	1996	1995
		(in millions)	
Pension expense:			
Service cost	$ 70	$ 72	$ 62
Interest cost on projected benefit obligation	308	309	304
Actual return on assets	(1,334)	(616)	(816)
Net amortization and deferral	899	217	450
Net pension (income) expense	$ (57)	$ (18)	$ —
Funded status:			
Actuarial present value of benefit obligations:			
Vested benefit obligation	$(3,770)	$(3,506)	$(3,256)
Nonvested benefits	(48)	(50)	(113)
Accumulated benefit obligation	(3,818)	(3,556)	(3,369)
Effects of projected future compensation	(391)	(401)	(323)
Projected benefit obligation	(4,209)	(3,957)	(3,692)
Plan assets at fair value	5,962	4,851	4,375
Excess of plan assets over projected benefit obligation	1,753	894	683
Unrecognized net gain	(1,536)	(770)	(627)
Unrecognized net obligation being amortized over 15 years beginning October 1, 1987	—	2	2
Prepaid pension cost	$ 217	$ 126	$ 58

The discount rate used to determine the actuarial present value of the projected benefit obligation was 8.0 percent in 1997 and 1996 and 7.5 percent in 1995. The assumed annual rates of increase in future compensation levels for 1997, 1996, and 1995 ranged from 3.3 to 8.3 percent. The expected long-term rate of return on plan assets was 11 percent for 1997, 1996 and 1995.

Other postretirement benefits

TVA sponsors an unfunded defined benefit postretirement plan that provides for contributions toward the cost of retirees' medical coverage. The plan covers employees who, at retirement, are age 60 and older (or who are age 50 and have at least five years of service). TVA's contributions are a flat dollar amount based upon the participants' age and years of service and certain payments toward the plan costs.

The annual assumed cost trend for covered benefits is 10.5 percent in 1997, decreasing by one-half percent per year reaching 5.0 percent in 2008 and thereafter. For 1996 and 1995, an annual trend rate of 11.0 percent and 11.5 percent, respectively, was assumed. The effect of the change in assumptions on a cost basis was not significant. Increasing the assumed health-care cost trend rates by 1 percent would increase the accumulated postretirement benefit obligation (APBO) as of September 30, 1997, by $15 million and the aggregated service and interest cost components of net periodic postretirement benefit cost for 1997 by $3 million.

The weighted average discount rate used in determining the APBO was 8.0 percent for 1997 and 1996, and 7.5 percent for 1995. Any net unrecognized gain or loss resulting from experience different from that assumed or from changes in assumptions, in excess of 10 percent of the APBO, is amortized over the average remaining service period of active plan participants. The following sets forth the plan's funded status at September 30:

	1997	1996	1995
	(in millions)		
Accumulated postretirement benefit obligation (APBO)			
Retirees	$220	$230	$214
Fully eligible active plan participants	2	4	1
Other active plan participants	126	187	116
APBO	348	421	331
Unrecognized net (loss) gain	—	(95)	(15)
Accrued postretirement benefit cost	$348	$326	$316
Net periodic postretirement benefit cost			
Service cost	$ 13	$ 8	$ 7
Interest cost	32	24	26
Amortization of loss	4	—	—
Net periodic postretirement benefit cost	$ 49	$ 32	$ 33

Other postemployment benefits

Statement of Financial Accounting Standards No. 112, *Employers Accounting for Postemployment Benefits* (SFAS No. 112), applies to postemployment benefits, including workers' compensation provided to former or inactive employees, their beneficiaries and covered dependents after employment but before retirement. Adoption of SFAS No. 112 in 1995 changed TVA's method of accounting from recognizing costs as benefits are paid to accruing the expected costs of providing these benefits. This resulted in recognition of an original transition obligation of approximately $280 million. During 1996, TVA made adjustments to certain assumptions utilized in the determination of the obligation at September 30, 1996, which resulted in an increase in the original transition obligation of approximately $194 million. In connection with the adoption of SFAS No. 112, and related approval by its Board of Directors, TVA recorded the transition obligation as a regulatory asset. The regulatory asset is being amortized over approximately 15 years, whereby the annual expense will approximate the expense that would be recorded on an as-paid basis.

Early-out and accelerated severance packages

In 1997, 1996 and 1995 TVA provided both voluntary and involuntary severance packages, which affected an aggregate of approximately 4,900 employees. During this period, severance costs totaled approximately $196 million and consisted primarily of severance pay ($150 million) and other retirement and postretirement benefits ($46 million). Also during 1997 TVA recognized a related pension curtailment gain of $27 million. The aggregate costs of the severance packages have been charged to the power program primarily as other expense during 1997, 1996 and 1995 in the amounts of $11 million, $35 million and $136 million, respectively, and the non-power program as non-power expense during 1997 and 1996 in the amounts of $8 million and $6 million, respectively.

9. MAJOR CUSTOMERS

One municipal customer accounts for approximately 9 percent of total power sales and four other municipal customers account for an additional aggregate 19 percent of total power sales. These five municipal customers purchase power from TVA under long-term contracts for terms of 20 years, which require 10-years notice to terminate.

10. CONSTRUCTION EXPENDITURES AND COMMITMENTS AND CONTINGENCIES

Construction expenditures

Construction expenditures, including capitalized interest, are estimated to be approximately $732 million for 1998 and $659 million for 1999. These estimates are revised periodically to reflect changes in economic conditions and other factors considered in their determination.

Purchase commitments

TVA has entered into approximately $2.3 billion in long-term commitments ranging in terms of up to eight years for the purchase of coal.

Contingencies

Nuclear insurance. The Price-Anderson Act sets forth an indemnification and limitation of liability plan for the U.S. nuclear industry. All Nuclear Regulatory Commission (NRC) licensees, including TVA, maintain nuclear liability insurance in the amount of $200 million for each plant with an operating license. The second level of financial protection required is the industry's retrospective assessment plan, using deferred premium charges. The maximum amount of the deferred premium for each nuclear incident is approximately $79 million per reactor, but not more than $10 million per reactor may be charged in any one year for each incident. TVA could be required to pay a maximum of $474 million per nuclear incident on the basis of its six licensed units, but it would have to pay no more than $60 million per incident in any one year.

In accordance with NRC regulations, TVA carries property and decontamination insurance of $1.06 billion at each licensed nuclear plant for the cost of stabilizing or shutting down a reactor after an accident. Some of this insurance may require the payment of retrospective premiums of up to a maximum of approximately $34 million.

Clean Air legislation. The Clean Air Act Amendments of 1990 require fossil-fuel fired generation units to reduce their sulfur dioxide and nitrogen oxide emissions in two phases in order to control acid rain. The Phase I compliance period commenced on January 1, 1995, for sulfur dioxide and January 1, 1996, for nitrogen oxide, while the Phase II compliance period commences on January 1, 2000. Based on the level of emissions, 26 of TVA's 59 operating coal-fired units are classified as Phase I units, with the remaining units being Phase II units. Compliance with these requirements has resulted in substantial expenditures for the reduction of emissions at TVA's coal-fired generating plants.

TVA's compliance strategy to reduce sulfur dioxide emissions includes the use of scrubbers at six fossil units and the use of lower-sulfur coal at the remaining 53 fossil units. TVA has completed all planned scrubbers and is on schedule to complete the change-over to lower-sulfur coal.

Nitrogen oxide reductions are required for 19 of TVA's Phase I units. These reductions were achieved through the installation of low-nitrogen-oxide burners at 13 units. TVA is in compliance with all Phase I requirements and is currently installing nitrogen oxide reduction equipment to bring TVA's remaining units in compliance with Phase II nitrogen oxide emission requirements.

Expenditures related to the Clean Air projects during 1997 and 1996 were approximately $40 million and $80 million, respectively. TVA has already completed the actions necessary to achieve Phase I compliance for both sulfur dioxide and nitrogen oxide emissions, and TVA is proceeding to take actions to comply with Phase II requirements that become effective in the year 2000 or after. The total cost of compliance cannot reasonably be determined at this time because of the uncertainties surrounding final Environmental Protection Agency regulations, resultant compliance strategy, potential for development of new emission control technologies and future amendments to the legislation.

Hazardous substances. The release and cleanup of hazardous substances are regulated under the Comprehensive Environmental Response, Compensation, and Liability Act. In a manner similar to other industries and power systems, TVA has generated or used hazardous substances over the years. TVA has been identified as a potentially responsible party with respect to three off-site disposal areas. TVA's liability at these sites has not yet been determined. In addition, TVA is currently investigating two other sites that TVA either owns or partially owns. TVA may have cleanup responsibilities at those sites by virtue of its control of the property. TVA's potential liabilities for its share of cleanup costs at these sites are uncertain but are not expected to be substantial.

Pending litigation. TVA is a party to various civil lawsuits and claims that have arisen in the ordinary course of its business. Although the outcome of pending litigation cannot be predicted with any certainty, it is the opinion of TVA counsel that the ultimate outcome should not have a material adverse effect on TVA's financial position or results of operations.

Decommissioning costs. Provision for decommissioning costs of nuclear generating units is based on the estimated cost to dismantle and decontaminate the facilities to meet NRC criteria for license termination. At September 30, 1997, the present value of the estimated future decommissioning cost of $318 million was included in other liabilities. The decommissioning cost estimates from a 1995 study are based on prompt dismantlement and removal of the plant from service. The actual decommissioning costs may vary from the estimates because of changes in the assumed dates of decommissioning, changes in regulatory requirements, changes in technology and changes in costs of labor, materials and equipment.

TVA maintains an investment trust fund to provide funding for the decommissioning of nuclear power plants. In September 1993, TVA sold the investment portfolio and realized a gain of $163 million. TVA sold the investment portfolio and realized a gain of $163 million. TVA recognized $82 million of this gain in 1994 and $81 million in 1995. During 1996, TVA took a number of related actions to establish a decommissioning fund that could reasonably be expected to provide substantially all of the funding required for decommissioning. TVA contributed an additional $123 million, and separate decommissioning trusts were established for each of TVA's nuclear plants. As of September 30, 1996, the entire fund was invested in equity market index funds.

In May 1997, TVA sold the entire $402 million equity index fund portfolio and transferred the proceeds to trust portfolios managed by independent money managers. During 1997, TVA recognized $151 million of income related to the fund, which included an $81 million gain on the sale of fund investments and $70 million in net appreciation and interest income. As of September 30, 1997, the decommissioning trust fund investments totaled $553 million and were invested in securities designed to achieve a return in line with overall equity market performance.

Cost-based regulation. As a regulated entity, TVA is subject to the provisions of SFAS No. 71, *Accounting for the Effects of Certain Types of Regulation.* Accordingly, TVA records certain assets and liabilities that result from the effects of the ratemaking process that would not be recorded under generally accepted accounting principles for non-regulated entities. Currently, the electric utility industry is predominantly regulated on a basis designed to recover the cost of providing electric power to its customers. If cost-based regulation were to be discontinued in the industry for any reason, profits could be reduced and utilities might be required to reduce their asset balances to reflect a market basis less than cost. Discontinuance of cost-based regulation would also require affected utilities to write off their associated regulatory assets. Such regulatory assets for TVA total approximately $1.9 billion at September 30, 1997, along with approximately $6.3 billion of deferred nuclear plants. Management cannot predict the potential impact, if any, of these competitive forces on TVA's future financial position and results of operations. However, TVA continues to position itself to effectively meet these challenges by maintaining prices that are locally, regionally and nationally competitive.

11. NON-POWER PROGRAMS

TVA's non-power programs provide various public services, including managing navigable river channels, providing flood control and overseeing certain recreation facilities. The non-power programs encompass general stewardship of land, water and wildlife resources. TVA's non-power programs also conduct certain research and development activities in pollution prevention and remediation.

Funding for the non-power programs is primarily provided through federal appropriations. During 1997 and 1996, the non-power programs received appropriations of $106 million and $109 million, respectively. The 1998 appropriations bill approved $70 million for non-power programs in 1998 and anticipates no further appropriation to TVA thereafter. Certain non-power program activities are also funded by user fees and outside services revenues. Notwithstanding the historical separation of the power and non-power programs and provisions of the TVA Act and bond covenants to the contrary, public law authorizes TVA to use power revenues to pay for non-power activities beginning in 1999.

During 1995, the non-power programs had a net expense of $182 million, which included a $69 million charge for the write-off of the Columbia Dam and Reservoir project. The Columbia Dam and Reservoir, a multi-purpose project financed by congressional appropriations, was suspended in prior years due to budget restrictions and environmental concerns. During 1995, TVA determined that the Columbia Dam would not be completed, and accordingly, the project cost was expensed.

The completed plant of the non-power programs consists of multipurpose dams and other plant. At September 30, 1997, the net completed plant balances for multipurpose dams and other plant were $700 million and $113 million, respectively. At September 30, 1996, the net completed plant balances for multipurpose dams and other plant were $705 million and $108 million, respectively.

REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Directors of the Tennessee Valley Authority

We have audited the accompanying balance sheets (power program and all programs) of the Tennessee Valley Authority as of September 30, 1997 and 1996, and the related statements of income (power program), changes in proprietary capital (power program and non-power programs), net expense (non-power programs) and cash flows (power program and all programs) for each of the three years in the period ended September 30, 1997. These financial statements are the responsibility of the Tennessee Valley Authority's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards and Government Auditing Standards issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the power program and all programs of the Tennessee Valley Authority as of September 30, 1997 and 1996, the results of operations of the power program and nonpower programs and cash flows of the power program and all programs for each of the three years in the period ended September 30, 1997, in conformity with generally accepted accounting principles.

As discussed in note 8 to the financial statements, in 1995 the Tennessee Valley Authority adopted Statement of Financial Accounting Standard No. 112, *Employers Accounting for Postemployment Benefits.*

In accordance with Government Auditing Standards, we have also issued a report, dated October 23, 1997, on our consideration of the Tennessee Valley Authority's internal controls over financial reporting and our tests of compliance with certain provisions of laws, regulations, contracts and grants.

Coopers & Lybrand L.L.P.
Knoxville, Tennessee
October 23, 1997

REPORT OF MANAGEMENT

Management is responsible for the preparation, integrity, and objectivity of the financial statements of the Tennessee Valley Authority as well as all other information contained in the annual report. The financial statements have been prepared in conformity with generally accepted accounting principles applied on a consistent basis and, in some cases, reflect amounts based on the best estimates and judgments of management, giving due consideration to materiality. Financial information contained in the annual report is consistent with that in the financial statements.

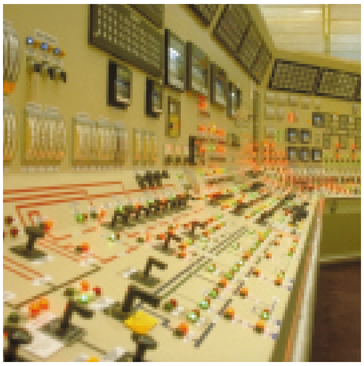
The Tennessee Valley Authority maintains an adequate system of internal controls to provide reasonable assurance that transactions are executed in accordance with management's authorization, that financial statements are prepared in accordance with generally accepted accounting principles, and that the assets of the corporation are properly safeguarded. The system of internal controls is documented, evaluated, and tested on a continuing basis. No internal control system can provide absolute assurance that errors and irregularities will not occur due to the inherent limitations of the effectiveness of internal controls; however, management strives to maintain a balance, recognizing that the cost of such a system should not exceed the benefits derived. No material internal control weaknesses have been reported to management.

Coopers & Lybrand L.L.P. was engaged to audit the financial statements of the Tennessee Valley Authority and issue reports thereon. Its audits were conducted in accordance with generally accepted auditing standards. Such standards require a review of internal controls and an examination of selected transactions and other procedures sufficient to provide reasonable assurance that the financial statements neither are misleading nor contain material errors. The Report of Independent Accountants does not limit the responsibility of management for information contained in the financial statements and elsewhere in the annual report.

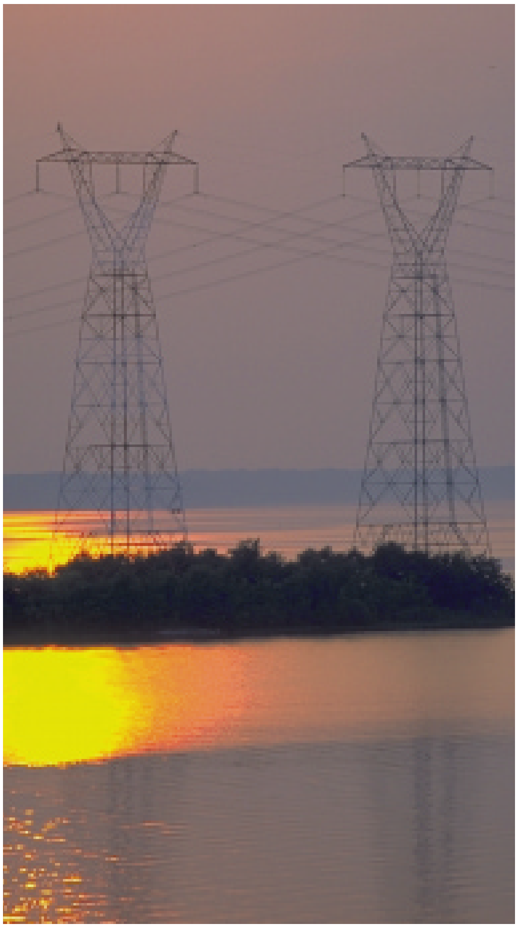
David N. Smith
Chief Financial Officer
and Executive Vice President of Financial Services

To be the recognized world leader in providing energy and related services, independently and in alliances with others, for society's global needs.

TVA is one of the largest power producers in the United States.



TVA's electric generation facilities include state of the art computer controlled production.



TVA's 16,600-mile system of transmission lines through seven states serves as a vital part of the United States energy infrastructure.

TVA is environmentally sensitive in managing the thousands of acres along the Tennessee River system.

The energy right *program was developed jointly by TVA and its customers to promote energy conservation through more efficient power use.*

TVA manages the nation's fifth largest river system for flood control, navigation, power production and recreation.

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